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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK
Case No. 08-13555 (JMP)
Case No. 08-01420 (JMP) (SIPA)
Adv. Case No. 09-01728

- - - - -x

In the Matter of:
LEHMAN BROTHERS HOLDINGS INC., et al.,
Debtors.

- - - - -x

In the Matter of:
LEHMAN BROTHERS INC.,
Debtor.

- - - - -x

MICHIGAN STATE HOUSING DEVELOPMENT
AUTHORITY,
Plaintiff,

- against -

LB DERIVATIVE PRODUCTS INC., et al.,
Defendants.

- - - - -x

(cont'd. on next page)

1 U.S. Bankruptcy Court
2 One Bowling Green
3 New York, New York
4

5 September 22, 2010

6 10:02 AM
7

8 B E F O R E:

9 HON. JAMES M. PECK

10 U.S. BANKRUPTCY JUDGE
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2 STATUS CONFERENCE

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4 HEARING re Motion for Authorization to Reject Certain Executory
5 Contracts [Docket No. 11201]

6
7 HEARING re Motion of Taipei Fubon Commercial Bank Co., Ltd.
8 Seeking Authority to Assign its Interests as Lender in a
9 Promissory Note Issued by Lehman Brothers Holdings Inc. [Docket
10 No. 11051]

11
12 HEARING re Debtors' Motion for Approval of (I) A Settlement
13 Agreement between the Debtors and Aurora Bank FSB Regarding the
14 Master Forward Agreement and Other Matters and (II) Certain
15 Other Related Relief, Including Authorization of (A) Certain
16 Debtors to Make Capital Transfers, (B) LBHI to Enter into a
17 Capital Maintenance Agreement, and (C) LBHI to Extend the
18 Duration of the Amended Repurchase Agreement and Financing
19 Facility [Docket No. 11141]

20
21 HEARING re Debtors' Motion for Approval of (I) a Settlement
22 Agreement between the Debtors and Woodlands Commercial Bank and
23 (II) Certain Related Relief, including Authorization of (A)
24 Certain Debtors to Make Capital Transfers and (B) LBHI to Enter
25 Into a Capital Maintenance Agreement [Docket No. 11142]

1
2 HEARING re Motion of Lehman Commercial Paper Inc. for Approval
3 of that Certain Amended and Restated Compromise by and Among
4 Lehman Commercial Paper Inc., Alfred H. Siegel, as Chapter 11
5 Trustee for the SunCal Debtors, and the Official Committee of
6 Unsecured Creditors in the SunCal Bankruptcy Cases [Docket No.
7 11153]

8
9 HEARING re Motion of the Chapter 11 Trustee of the SunCal
10 Master Debtors for Relief from the Automatic Stay [Docket No.
11 9642]

12
13 HEARING re Michigan State Housing Development Authority v. LB
14 Derivative Products Inc., et al. [Adv. Case No. 09-01728]
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24 Transcribed By: Clara Rubin and Sharona Shapiro
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1 P R O C E E D I N G S

2 THE COURT: Be seated, please.

3 Good morning, Mr. Miller.

4 MR. MILLER: Good morning, Your Honor. There's --

5 THE COURT: Before you start, let me just make an
6 announcement for those people who are standing in the aisles.
7 We really do have adequate overflow capacity upstairs, and I
8 don't think if you're going to be sitting there you're going to
9 miss anything. You'll certainly be able to hear and see what's
10 on video. If you were actually planning to participate in the
11 substance of the hearing later, I'm going to take maybe a
12 five-minute break after the State of the Estate report to allow
13 people to reassemble. So anybody's who's on the seventh floor
14 who needs to participate or wants to observe in person the
15 later proceedings will have an opportunity to come back. I'm
16 just, frankly, concerned about the comfort of the crowd and
17 encourage you to move, but I'm not going to force you to move.
18 It'd be great if somebody actually follows that suggestion.

19 Thank you, the one person who left.

20 MR. MILLER: There is a rumor, Your Honor, this is
21 being streamed into Times Square.

22 THE COURT: That's a completely false rumor, as far as
23 I know.

24 MR. MILLER: Good morning, Your Honor. Harvey Miller,
25 Weil, Gotshal & Manges, on behalf of the debtors.

1 Your Honor, we have on the agenda for this morning as
2 the first matter a status conference, which has been entitled
3 "State of the Estate Presentation". And before we get to it,
4 Your Honor, I'd like to make a few introductory remarks.

5 It has been a little over two years since the
6 commencement of these huge totally unplanned Chapter 11 cases
7 that have affected the lives of so many persons and threatened
8 the viability of the financial system, the global financial
9 system, cases that have spawned over eighty foreign insolvency
10 proceedings and have accentuated the need for a global system
11 to deal with interconnected insolvency cases. The primary
12 case, Lehman Brothers Holdings Inc., started with little
13 appreciation of how the assets of the Lehman enterprise and its
14 broker-dealer subsidiary Lehman Brothers Inc. would be salvaged
15 and values preserved.

16 The Court aptly described Lehman as having been
17 overcome by a tsunami of the most gigantic proportions.
18 Whatever else may be stated, I believe it is beyond dispute
19 that Lehman was the spark that ignited the financial collapse
20 that almost brought down Morgan Stanley & Co. and even the
21 mighty Goldman Sachs, and did cause the AIG bailout and the
22 merger of Washington Mutual Savings into Wachovia. It was a
23 major precipitating factor in the enactment of the Dodd-Frank
24 Financial Reform Act of 2010.

25 Lehman has made the phrase "too big to fail" a part of

1 the lexicon -- everyday lexicon of the United States Congress,
2 the Internet and the media. The debate over the demise of the
3 Lehman enterprise was the result of egregious miscalculation on
4 the part of the Federal Reserve Bank, the United States
5 Treasury and others. That debate continues unabated.

6 The Financial Crisis Inquiry Commission was appointed
7 during 2009 to undertake an investigation into the causes of
8 the financial crisis of 2008. That commission's report is
9 scheduled to be filed in December of this year. In testimony
10 before that commission two or three weeks ago, Chairman
11 Bernanke testified that the Federal Reserve Bank seriously
12 miscalculated the consequences of Lehman's collapse. He also
13 defended the decision to strictly construe Section 13(3) of the
14 Federal Reserve Act as having presented an absolute bar to any
15 federal assistance to soften the effects of Lehman's bankruptcy
16 on the world financial system.

17 By my count, there are at least twenty-five books that
18 have been published since January 2009, setting forth the
19 alleged facts and hypotheses as to the circumstances and
20 reasons why Lehman collapsed in the manner in which it did.
21 Much has been written, particularly by the participants in the
22 decision-making process in the fall of 2008; constitutes
23 revisionist history. It reminds one of the debate Winston
24 Churchill was having with an adversary in the House of Commons,
25 in response to criticisms of actions he was taking as prime

1 minister of the United Kingdom. Churchill loudly explained
2 'History will prove I am right. I know that, for I will write
3 the history.' So much for former Secretary Paulson's book "On
4 the Brink".

5 There have been at least three extensive TV
6 documentaries centered on the financial collapse of the Lehman
7 enterprise. On October 1st of this year, the New York Film
8 Festival will present a documentary entitled "Inside Job" which
9 covers the planting of the seeds of the financial disaster, the
10 insatiable greed that led to more and more risk-taking and the
11 eventual bursting of the bubble. A good portion of the film
12 deals with Lehman's contribution to a market built on excessive
13 debt, short-term credit and deregulation that betrayed public
14 trust.

15 In that context, the past two years have been crammed
16 with intensive dedication on the part of many, many persons to
17 retrieve, preserve and enhance the value of the Lehman
18 enterprise so that a fair Chapter 11 plan may be proposed that
19 will equitably distribute the asset values that had been
20 created by the dedication of the persons who have been
21 administering these cases.

22 The docket sets forth the numerous proceedings that
23 have been brought in this court, proceedings that have taken
24 hours and hours of dedicated time of persons involved, and of
25 the Court. Yet those proceedings are but the tip of the

1 iceberg and do not adequately describe the day-to-day
2 activities that go on at the Lehman offices and in the offices
3 of the professionals engaged by Lehman and others in the search
4 for assets values and protection of the debtors' interest and,
5 therefore, creditor interests.

6 These are the most complex and difficult cases to ever
7 enter the bankruptcy stream. They are spiced with esoteric
8 financial transactions and securities, global considerations,
9 intercreditor disputes and issues, conflicts of laws, and
10 almost every problem that one might conceive. Nonetheless,
11 significant progress has been made, albeit at substantial cost
12 of administration, which the media is so happy to point out and
13 elaborate.

14 I take comfort in the words of Professor Douglas Baird
15 who responded to media inquiries as to fees by essentially
16 asking that there be a realistic analysis of the aggregate fees
17 in the context of the value of the assets administered and
18 ultimately the success of the administration.

19 Two years is a relatively short period of time in the
20 perspective of the cases of the magnitude and complexity of
21 these cases. The provisions of the Bankruptcy Code, when
22 adopted, did not contemplate such cases. It has been almost
23 unanimously agreed that the eighteen-month limitation on the
24 proposal of a Chapter 11 plan doesn't really fit these cases.
25 And the same might very well apply to the statute of

1 limitations for avoidance actions that are set forth in Section
2 546 of the Bankruptcy Code.

3 Indeed it took the examiner over fourteen months to
4 complete and file his report in March of this year, at a cost
5 of almost 105 million dollars. As I am sure the Court has
6 noted, September 15, 2010, just seven days ago, a large -- I'm
7 sorry, just seven days ago, a large number of adversary
8 proceedings, based upon the avoidance powers under the
9 Bankruptcy Code, were initiated in this court. In addition,
10 the debtors-in-possession have entered into a large number of
11 agreements with potential adversaries to toll the otherwise
12 applicable statutes of limitations for the commencement of
13 recovery actions.

14 Undoubtedly there will be significant litigation
15 augmenting the substantial litigation that has already been
16 commenced and is pending before the Court. However, the
17 objective is that economic compromise should be the basic
18 guideline to the resolution of issues and the formulation of an
19 amended Chapter 11 plan that will fairly deal with the claims
20 of all constituencies and avoid the excessive costs of
21 litigation and the time that may be consumed by such
22 litigation.

23 As has been the practice for the past two years, and
24 in response to the Court's request, the debtors'
25 administrators, led by Mr. Bryan Marsal and Mr. John Suckow,

1 will present today what has been characterized as "The State of
2 the Estate". (It's interesting that it's on the same day that
3 President Obama is doing something of that character.) It is a
4 continuation of prior similar reports that were made to the
5 Court over the past two years.

6 Unless the Court has questions, I would propose to
7 turn the lectern over to Mr. Marsal to commence the report.

8 THE COURT: Thank you, Mr. Miller.

9 Mr. Marsal, the floor is yours.

10 MR. MARSAL: Good morning, Your Honor.

11 THE COURT: Good morning, Mr. Marsal.

12 MR. MARSAL: Your Honor, I just want to make sure the
13 audience and you understand that, beginning with the
14 commencement of this presentation, the company is
15 simultaneously filing a Form 8-K with the SEC and is also
16 making this entire presentation available on its Web site. So
17 as of right now, everything that's going to be shown is
18 available to the public.

19 THE COURT: But no streaming video of you?

20 MR. MARSAL: No. No, sir. No streaming video, I
21 hope. I hope.

22 What we'd like to cover with you today, Your Honor, is
23 really a summary of what we've been doing the last two years,
24 covering the assets -- the asset recovery efforts, the claims
25 resolution efforts and, finally, the plan of reorganization,

1 which I believe I promised you about a week ago. So we will
2 see where we are in that entire process.

3 Going to the executive summary, this case, as Mr.
4 Miller points out, is a highly complex case which I think has
5 advanced significantly over the last -- since the last State of
6 the Estate. The market for the various assets of the
7 company -- liquidity has improved, refinancings has improved,
8 and we've been employing, along with the improvement in the
9 market, an aggressive asset recovery strategy, reinvesting in
10 assets, completing assets that were either work-in-process or
11 identifying control positions, trying to obtain those positions
12 we think has proven to be a very effective strategy in
13 maximizing the recovery value.

14 By the final bar date in November, we received 1.2
15 trillion dollars of claims filed. Significant progress has
16 been made, as you'll see later in the presentation, on that 1.2
17 trillion. Today at the holdings level, we are down to in the
18 neighborhood of 260 to 360 million dollars' worth of --
19 billion, excuse me, worth of claims. That's still a large
20 number, and much work to be done, but you'll see, I think, that
21 significant progress has been made.

22 We filed the plan, a directional plan, on the -- in
23 March, followed by a disclosure statement in April. And we
24 believe that creditor differences have been significantly
25 narrowed over the course of time since that -- since coming out

1 with that original plan.

2 Moving on to specifics, every asset team -- and,
3 again, if you recall, we divide the estate into five assets
4 teams; each of those assets have updated their recovery
5 analysis from the April presentation, the April disclosure
6 statement. Every one of those teams is coming in with higher
7 recovery values. The markets continue to stabilize, and values
8 in pricing is improving. Again, we would emphasize that our
9 liquidation strategy, which has been supported, most
10 importantly, by the unsecured creditors' committee, is focused
11 on the creation of value as opposed to the creation of
12 immediate cash, which is -- which I think will pay significant
13 dividends to the estate.

14 We've worked out a deal with the FDIC, which we
15 believe will optimize the liquidation recovery from the bank
16 platforms. Where appropriate, and I'm sorry about this one
17 because I know you've got a lot on your docket, but we have --
18 we're pursuing significant lawsuits against some of the
19 clearing banks, against Barclays, and clearly there is a slew
20 of potential avoidance actions out there that we filed with the
21 Court or received tolling agreements on.

22 On the foreign administrative front, I'm happy to
23 report that that relationship has improved over the course of
24 two years. We're really working together now. I wish it had
25 been earlier, but it's working well now. And I think that

1 you're going to see, as you'll see later in our presentation,
2 improvement in recovery values because of that.

3 We have a good relationship with LBI, but I'm still
4 very much in the dark. I'm very much in the dark what's going
5 on at LBI, and I wish -- you know, I wish Mr. Miller had added
6 that to the things that need to be addressed about the
7 bankruptcy process, because --

8 THE COURT: Could you explain what you mean by --

9 MR. MARSAL: I --

10 THE COURT: -- by that?

11 MR. MARSAL: I just don't feel I know what's going on
12 in that estate, Your Honor. I don't understand how some of the
13 assets are being treated. And we continue to feel -- we just
14 continue to feel a bit in the dark, and I don't know what I can
15 do about it, but --

16 THE COURT: Well, only within the last month, I
17 believe, the LBI trustee filed a fairly extensive written
18 report, which I've had a chance to look at. I'm sure you've
19 seen the report as well. I'm frankly surprised at that
20 comment, both given the content of that report and given the
21 parallel fiduciary duties of the two estate administrators.
22 But we can talk some more about that another time.

23 MR. MARSAL: Yeah, I will -- yeah, it's not a
24 complaint. We have a good relationship, Your Honor, but
25 there's just lots of information lacking from our team -- from

1 various teams' perspective on --

2 THE COURT: Is that because the information is not
3 available or because the information is not being shared?

4 MR. MARSAL: I don't know which. There is
5 cooperation, Your Honor. I don't know whether it's available,
6 but there is cooperation, but we just have -- after two years,
7 I wouldn't have expected to have some of the holes that we have
8 in our fact base --

9 THE COURT: Okay.

10 MR. MARSAL: -- that we have today. But, again, I
11 think -- I don't want to harp on it, because I'm eighty percent
12 happy and twenty percent unhappy, if you would.

13 Last but not least, on the JPMorgan front, very
14 helpful in getting that out of the way. We have -- that has
15 cleared up some of the -- cleared up our ability to dispose of
16 some of the assets as to the removal of the liens. So that,
17 again, is helping the overall administration of the case.

18 Next item on the exec summary is claims management.
19 Originally 860 billion in claims were filed at LBHI, and 302
20 billion at the various subsidiaries. After cleaning up errors
21 and dupes, we believe that the unsecured claims at LBHI are
22 closer to 250 to 350 billion. Our target right now -- we
23 believe that the number will ultimately come out closer to 250
24 to 260 billion in claims, but we still have that kind of a
25 range to work on, which is with the additional analysis that's

1 needed. We also are in a position -- because of getting the
2 claims more in order, we think we now are in a position to
3 really have a plan where we know who could vote on a plan as to
4 who has a legitimate claim, if you would.

5 The key priority of the last six months has been to
6 focus on the foreign receivers. And, again, I think we've made
7 significant progress on that front.

8 In terms of case administration, Your Honor knows the
9 examiner's report was filed in March. We have a slew of
10 requests from various governmental agencies that -- prior to
11 this report and post this report, asking for information and
12 continue to support that effort. Full transparency in
13 communication with the UCC, U.S. Trustee, fee committee, that's
14 just ongoing. Financial reporting is timely and current.
15 Given the size and complexity of the cases involved, again, I
16 would consider this overall administration to be timely and
17 efficient.

18 In terms of the plan process, the original timetable,
19 as I said, was to try and complete -- to get a plan of
20 reorganization approved by the second anniversary. The biggest
21 obstacle to doing that is the foreign receivers. We
22 miscalculated as to how long it was going to take us to first
23 of all educate them on the Chapter 11 process and our issues,
24 then have them go back to their various constituencies and
25 explain to them the issues, explain to their creditors the

1 issues, and then to come back to us with a counterproposal.
2 That process has been somewhat time-consuming and slow and,
3 particularly if you happen to be domestic creditor, you're a
4 little frustrated by this. We've urged everyone to be patient
5 because it's a lot better than the alternative, which we think
6 is a litigation, which will get us nowhere and at least will
7 delay the process even further.

8 THE COURT: I don't want to interrupt your flow --

9 MR. MARSAL: Yes, sir.

10 THE COURT: -- but can you tell me how the
11 multilateral protocol is functioning and whether or not that's
12 a meaningful contributor to improved relations?

13 MR. MARSAL: It is, Your Honor, in that -- I mean, no
14 one is -- obviously, no one is going to jeopardize their
15 sovereign rights to apply whatever principles they have in
16 their country. But even LBIE, despite not being a direct
17 participant in the protocol, is in fact operating as if it were
18 a participant in the protocol. So I think it's been very
19 effective in terms of communication.

20 The first six months were rough. The next six months
21 got better. The last twelve months it's been pretty good; lots
22 of cooperation among the receivers. And, in fact, later on
23 today we're going to announce that we reached our first
24 settlement with the largest -- with one of the largest
25 receivers, and we would hope to have that be the first of a

1 number of settlements which will be before the Court. And,
2 again, I don't want to jump ahead, but we'll talk about that
3 later. That's been the biggest handicap was the foreign
4 receivers.

5 We are anticipating that we're going to file a new
6 disclosure statement by the -- sometime in the fourth quarter
7 of this year, and we will be seeking a plan to be approved,
8 hopefully plan confirmation, in the first quarter of 2011.
9 Again, that's aggressive, and I've been cautioned by Mr. Miller
10 not to say that, but trying to drive an organization toward a
11 realistic date, and I think it's realistic subject to,
12 obviously, some of the other parties going along with it, but I
13 think there is momentum in the case to get the case resolved,
14 at least as a -- resolved as it relates to the claims.

15 Moving on to the specific assets, our cash position as
16 of the end of June -- well, this is significantly higher today,
17 but, again, to try and -- we have a June 30th cutoff date. If
18 you look over to your right, Your Honor, you'll see 18 billion
19 in cash -- 18.9 billion in cash, with 2.2 billion in posted
20 pre-petition cash collateral; that's principally at Citibank.

21 THE COURT: If you were to update that to today's
22 number or something around today's number, what would you be
23 talking about in terms of an order of magnitude of cash on
24 hand?

25 MR. MARSAL: I would --

1 MR. MILLER: Another billion to billion and a half,
2 Your Honor.

3 MR. MARSAL: Another billion to billion and a half,
4 Your Honor.

5 THE COURT: So we're talking maybe twenty-two and a
6 half to twenty-three billion?

7 MR. MARSAL: Yes.

8 THE COURT: Okay.

9 MR. MARSAL: Yes. In terms of -- the next slide, this
10 is -- I wanted to identify what the sources of that cash flow
11 have been. The total sources of cash, 25.9 billion dollars,
12 coming -- the biggest single source is derivatives. There's
13 been uses of cash, operating expenses, 1.6 billion; again, that
14 would represent about eighteen months' worth of expenses, to
15 give you a run rate of how we are spending money today. And
16 the -- you see the Bankhaus settlement of 1.28 billion dollars.
17 So in total our uses of cash are 7.9 billion, resulting in the
18 18 billion dollars on the previous page.

19 Okay.

20 In terms of the first category of key assets, loans,
21 we had a large portfolio. We were simply a commercial lender.
22 The market continues to improve in this area. Refinancings are
23 happening actually ahead of schedule. While we're not seeing
24 more dollars, we're seeing an acceleration of the repayments,
25 which is the good news. So from a

1 present-value standpoint, this is improving.

2 Unfunded revolvers: We have eliminated twenty-six
3 billion of unfunded revolvers at a minimal cost to the estate.
4 That's about eighty-five percent completed, and I would expect
5 that this will be -- at a timely filed plan, this will be a
6 nonissue, any unfunded responsibility or problem.

7 Our strategy in loans has been to continue to rely on
8 an improving liquidity position. Again, with the support of
9 the unsecured committee, we've been pretty successful in
10 creating value there as opposed to blowing out positions today.

11 Next.

12 On the derivative front, we are increasing the
13 estimate of gross recovery proceeds by 850 million dollars.
14 And I'm cautiously optimistic that the next time we report on
15 this, this will in fact be better than the 850 million we're
16 talking about here. But all the -- we expect to collect
17 fifteen billion from derivatives from all the various receivables
18 being managed or being supervised by LAMCO. LAMCO is actively
19 hedging some of the positions in order to lock up the contract
20 values. I mean hedging the positions not to -- not for
21 purposes of making money; just to make sure that we have those
22 values locked up.

23 Big bank -- the big issue with derivatives is
24 resolution of the big-bank claims. That remains a major
25 challenge in 2011. It shouldn't get in the way of a plan, but

1 it will take some time. As I think I've said in the past, Your
2 Honor, this is a situation where very aggressive files (sic)
3 have been claimed and lots of homework has to be done to
4 support those claims.

5 The last shot there. The derivative team has done a
6 terrific job. They've surpassed all of our expectations and
7 have outperformed internal targets.

8 On the private equity front, again, much of this
9 private equity was created -- what Lehman would do is Lehman
10 would -- as they raised a fund for a private-equity firm, they
11 would always take a piece of the fund as an LP. And so what
12 we're left with is many, many of these limited partnership
13 interests in various funds. The guy putting the deal together
14 would get the bonus and we would be stuck with the long-term
15 play of this private equity investment, unfortunately. That's
16 going to take a long time to wind down.

17 Having said that, though, market conditions are
18 better. The disposition and pricing on those assets are
19 improving. The portfolio's up about two percent since April.
20 And the team really has a pretty good understanding of the exit
21 strategy. And, again, I'm pretty pleased with what's going on
22 from that team.

23 THE COURT: Just a question on that.

24 MR. MARSAL: Yes.

25 THE COURT: Is the thought to endeavor to monetize

1 those positions, or simply to hold onto them and hope for the
2 best?

3 MR. MARSAL: Well, it varies, Your Honor. In some
4 instances, the -- it depends on the age of the fund. If the
5 fund has an exit with an eight-year strategy, we would probably
6 hang onto it if we're in the eighth -- seventh year, let's say.
7 If we're -- if it has an eight-year disposition strategy and
8 we're in the second year, we would be more prone to sell as
9 opposed to hold. It depends on each -- it depends on the
10 circumstances associated with each investment.

11 THE COURT: All right.

12 MR. MARSAL: In terms of real estate, the real-estate
13 gross proceeds have actually improved, in terms of our
14 analysis, a hundred million dollars, but significantly more
15 than that in terms of repayments are being accelerated in terms
16 of timing. And in the original proposal we made some mistakes
17 on the calculation of recovery value. So this masks some of
18 the correction of the mistakes that were made. So it's more
19 like about a half a billion dollars' worth of real-estate
20 improvement during this time period.

21 We are not calculating this go-round the unrecognized
22 upside in value. We're taking a more conservative posture on
23 that. And I believe that the LAMCO real-estate team has
24 finally moved from being originators of loans to loan workout
25 professionals, now to working the asset management

1 professionals. So there's been a -- you know, it's been a good
2 evolution.

3 You know, the -- again, I can't overstress, the
4 cooperation of the UCC has been vital in this process, because
5 we've done some unorthodox things on the real-estate front in
6 terms of reinvesting and trying to get control of a position so
7 that we can protect positions or to be able to take action.
8 And that's been very much appreciated.

9 On the bank platforms, which has, I know, been a real
10 thorn in the Court's side, us coming back continually on this,
11 finally got a deal with the FDIC. We think we're going to
12 realize at least a billion-and-a-half-plus over the next
13 eighteen months out of this. It also eliminates -- as Your
14 Honor will remember, there's a substantial priority claim by
15 the FDIC claimed if this thing were to go into liquidation, and
16 that becomes a nonissue.

17 On the foreign receivables side, there's an increase
18 of one billion dollars in gross recoveries that should be
19 anticipated. And a combination of just not having the facts --
20 we're getting -- again, as we get more cooperation, we
21 understand the asset side of the subsidiaries and how they're
22 doing better, of the receivers, not under -- I mean of the
23 foreign receivers, I should say.

24 In terms of litigation activities -- you're more
25 familiar with this than I -- we have a slew of them. The last

1 item on the avoidance actions and tolling agreements, those
2 total -- they have a notional value of five billion dollars
3 that we are pursuing, in addition to the three major cases of
4 Bank of America, Barclays, JPMorgan. This is not all the major
5 cases. There are other potential major cases which are being
6 tolled.

7 In terms of what does that all mean to us, what it
8 means is that on the disclosure statement in April, we outlined
9 net proceeds of 55.3 billion. Today the estate would say
10 that's it's more like 2.2 billion. And, again, that 55.3 was
11 probably overstated at that time, so the improvement is closer
12 to 3 billion dollars during the six-month period. And -- but
13 we're now looking at net proceeds of 57.5 billion; this is
14 after reinvestment, by the way, Your Honor -- second to last
15 line -- of 1.8 billion.

16 In terms of the legal -- the same 57.5 billion by a
17 legal entity, which would be undoubtedly of interest to the
18 various claimants, you see the 57.5 broken out by various legal
19 entity. Most of the reinvestment will be reinvestment in LBHI
20 assets.

21 Okay, the next slide covers headcount plan, how will
22 this -- how has this matter been executed. What you've got,
23 Your Honor, are three categories of activities: LAMCO, which
24 is really asset management; administration, which includes your
25 claims and your financials; and then litigation, which is all

1 the various actions we've got going on, along with forensic
2 activities.

3 We attempted to cross the horizontal axis to identify
4 three points in time, April '09, April '10 and April -- a
5 projected April '11, to give you an idea of how the estate will
6 be moving in terms of headcount. I don't -- you know, I mean,
7 the -- you've got -- what you see in the change between April
8 '09 and April '10 really reflects, again, the activity on the
9 claims side increasing, and the assets side decreasing, as it
10 relates to A&M, for example.

11 You see the derivative portfolio. Much of LAMCO will
12 be coming down as derivatives wind down. It's our objective,
13 Your Honor, that the 149 A&M employees that were on board April
14 10th -- excuse me, April of 2010, will be down to 66 by the
15 anniversary of that date, namely April 2011.

16 THE COURT: Does that assume confirmation of a plan in
17 the first quarter, or that's just a projected date that's
18 unrelated to that contingency?

19 MR. MARSAL: It's a projected date, Your Honor. I
20 didn't get quite so -- I got the dates from the operating
21 people, and maybe it hasn't been exactly coordinated, but
22 that's a directional. I mean, I would take it as directional.
23 There's one other problem you have here, and that is, as the
24 market improves, the people in legacy Lehman -- we run a risk
25 that those people are going to be leaving. And, I mean, we see

1 more and more people leaving the estate, and there is only one
2 failsafe and that's A&M filling the hole. So this assumes that
3 we can keep the people and we can identify some business in
4 LAMCO, for example, and hopefully give a -- you know, give them
5 the interest to both retention and give them a career path.
6 And if we can't do that, this projection could be in jeopardy.

7 THE COURT: Okay.

8 MR. MARSAL: Claims resolution side, as I indicated,
9 was filed, was 1.162 trillion dollars of claims, consisting of
10 LBHI of 860 billion and 302 of the -- that are subsidiaries.
11 The first cutout at adjusted claims -- when we got the first
12 cutout, which was by April, we said 'Wait a minute, this is way
13 overstated.' So the total claims, LBHI, was 605 and we felt
14 that the claims at the subsidiary level were about 135. At
15 that point in time, when we came out with the disclosure
16 statement, we came out with a third column, which is your
17 likely allowed claims; that reflects the numbers in the
18 disclosure statement of 395 billion, of which 260 would be at
19 LBHI.

20 The fourth column is -- after scrubbing it further, we
21 believe that the 740 billion of claims is now 464 billion. We
22 believe that LBHI, 605, is now down to 363. And we believe
23 that the -- that subsidiary claims are, from 135, down to 101.

24 The last column is where we think this is all going to
25 end up, and that is we think that at the end of the day we're

1 looking at something close to an LBHI claim of 264 and total
2 claims in the subsidiaries of 101 million, for a total of
3 365 -- I'm sorry -- million -- billion. I keep saying
4 "million" when I mean "billion". 365 billion. Any questions
5 on that, Your Honor?

6 THE COURT: I'm not going to ask you --

7 MR. MARSAL: Confusing?

8 THE COURT: -- how you make that projection, because
9 I'm assuming you have some kind of proprietary information.

10 MR. MARSAL: Yes, Your Honor. That would be -- it
11 would be inappropriate in this forum to discuss that, but yes
12 we do. Each of these have a -- we have a negotiation going on
13 is what I'm trying to say.

14 THE COURT: Fine. I accept this as your best estimate
15 of where --

16 MR. MARSAL: Yes.

17 THE COURT: -- this is going to end up.

18 MR. MARSAL: Best estimate.

19 Summary highlights. Although not adjudicated at this
20 point, substantial progress. We've brought it from 1.2
21 trillion down to 464 billion. The affiliate guaranty
22 outstanding claims are projected to decrease by 150 billion.
23 We think we have -- we're pretty close to getting agreement on
24 that from the various foreign subsidiary -- foreign
25 administrators. The same thing is true of third-party guaranty

1 claims. The estimate of direct claims -- we've actually
2 increased a reserve of ten billion dollars; that's -- that
3 is -- that again is a contingent reserve. As we get into the
4 negotiations with various parties, we believe some portion of
5 that ten billion will be needed, which is incorporated in our
6 estimate.

7 And then the intercompany claims. We feel pretty
8 comfortable with the intercompany claims, with one exception,
9 and that is LBT, where we have an active negotiation going on.
10 But, again, this is a work in process and -- but forty-three
11 billion is -- we think, continues to be a reasonable estimate.

12 In terms of the plan, the plan -- I think the key
13 parts of this is that there's a lot of cooks in this kitchen.

14 Can we go to that? Thank you.

15 There's a lot of cooks in the kitchen. In addition to
16 the UCC and the LBHI ad hocs and the LBSF ad hocs and the LBT
17 ad hocs and a number of foreign protocol administrators and
18 foreign administrators, LBIE and LBI, and various other inputs,
19 we have a lot of cooks in the kitchen who were commenting about
20 the structure and the construct of the plan. And we welcome
21 all the input and -- but clearly this just speaks to the size
22 of this case.

23 In terms of the key issues presented by the parties,
24 substantive consolidation versus nonsubstantive consolidation,
25 and we've done our review, we have -- you know, we see merit in

1 both arguments. The company, on the substantive consolidation
2 side, was operated as one company. It was -- again, it was
3 managed -- it really was not managed on a legal-entity basis.
4 Many of the subsidiaries had absolutely no employees, they had
5 no addresses, they had no physical locations. This was simply
6 an accounting entry. Again, the -- at the same time, having
7 said that, there were separate subsidiary financial statements,
8 and in fact the company had thirty comptrollers going into
9 vigorous detail on constructing these financial statements; we
10 think, mostly for tax purposes, but they went into extensive
11 detail on keeping the books and records separate. A vote in
12 favor of sub con.

13 There was a centralized cash management system and,
14 really, reliance -- there's no apparent -- as far as we can
15 see, there's no good argument made for a separate credit
16 analysis. There was one entity that we saw from a financial
17 credit analysis standpoint that people were looking to.

18 At the same time, we've interviewed subsidiary
19 creditors who assert that a double-dip claim's appropriate
20 because two's better than one, irrespective of the reliance
21 factor. They did rely on it, because it's better to get a
22 subsidiary guaranty than not to get a subsidiary guaranty, even
23 if they didn't have financials.

24 On the regulatory standpoint, it's pointed out by each
25 side that Lehman was subject to the CSE program, which means

1 global supervision of both the holding company and of LBI by
2 the SEC. And yet clearly -- you know, clearly, Lehman entities
3 were regulated by local law and by separate rules. So there's
4 pros and cons on both sides, and what we tried to do, we
5 listened to everyone.

6 Yes?

7 MR. MILLER: Your Honor, if I may interject. Insofar
8 as this presentation is concerned, this is intended just for
9 informational purposes. These are not intended to be binding
10 admissions against interests or anything of that kind, but just
11 for informational purposes in respect of this report.

12 MR. MARSAL: Thank you.

13 THE COURT: That cautionary note is understood and is
14 in the record, and I never assumed that this hot issue, which
15 is being highlighted at a very high level, is being resolved in
16 any manner or that there's any bias being shown in the chart,
17 either in favor of or in opposition to substantive
18 consolidation. I simply take this as a listing of some of the
19 consideration's pro and con.

20 MR. MILLER: Thank you, Your Honor.

21 MR. MARSAL: Thank you.

22 And going to the next -- having said the pros and
23 cons, what we said was we think the best way to go here is an
24 economic compromise plan which respects the individual
25 subsidiaries and their legal status, and yet there are

1 compromises that would be made to LBHI which would, again,
2 provide a basis for their waiving any claim to a substantive-
3 consolidation argument. We think that this economic
4 compromise, as pointed out below, will reduce the time and
5 costs and need to litigate a very, very thorny issue given --
6 many, many thorny issues on this topic, and really to try and
7 avoid the issue of having to deal with whether or not sub con
8 or not applies here. That is our objective is to come out with
9 an economic compromise which will make nobody happy but
10 everybody happy.

11 In terms of our priorities in the plan process, the
12 first group that we needed to attack was the international
13 affiliates. And like I said, Your Honor, we made significant
14 progress on that as of yesterday. We have an agreement in
15 principle with the German receiver, Bankhaus, which is an
16 important one -- it's the second largest of the receivers -- on
17 a settlement. And that settlement, though, is subject to us
18 going to -- is them going back to their creditors -- the
19 receiver going back to their creditors and us going back to the
20 unsecured creditors' committee as well as -- and that's come
21 before the Court.

22 We would hope that on the LBIE front, which is the
23 largest, we're making significant headway with LBIE, and I'm
24 cautiously optimistic that we will soon have something to
25 report on the LBIE front as well. So I think the foreign

1 receivers are coming along, and I think our patience is paying
2 off.

3 The point number 2, our second objective is to -- is
4 really to attack the direct claims of LBHI. That is underway,
5 how do we go from the 210 that are filed to our estimate of 112
6 billion.

7 The third priority is really to focus on the LBHI
8 direct creditors and the domestic creditors and the compromise
9 that would be made by the domestic creditors to the LBHI
10 estate. And those negotiations and discussions are ongoing.

11 At the same time, the fourth point, if we cannot reach
12 agreement, then, as Mr. Miller points out, we may be back with
13 a different alternative. But it's our hope that we can find a
14 compromise solution with the various parties.

15 Timetables: We are -- we hope to complete the
16 bilateral negotiations with the foreign affiliates in the next
17 sixty days. We will -- at the same time, we will be engaging
18 domestic stakeholders and trying to clean up the direct claims,
19 hopefully settling some of those -- some of the direct claim --
20 holdings direct claims, with an intention of filing a new
21 disclosure statement and having a plan confirmed by the end of
22 the first quarter. Obviously the key there will no longer be
23 the foreign administrators; after sixty days it will be whether
24 or not the domestic subsidiary creditors and LBHI can get
25 together on this compromise. And we are trying to be the

1 Honest John in bringing about that compromise.

2 Any questions, Your Honor?

3 THE COURT: I do have one question as it relates to
4 the last point you made concerning the potential time-consuming
5 problem of dealing domestically with the claims of creditors at
6 different subsidiary levels. A few months ago, partly as a
7 result of an objection that was filed by counsel for the ad hoc
8 committee in the parent case, there was some discussion on the
9 record of a protocol or some means to facilitate communication
10 in a formal way. I deferred action with respect to that and
11 left it to the debtors to propose something -- it doesn't need
12 to be publicly proposed -- that would satisfy some of the
13 concerns that had been expressed on the record at that time.
14 In fact, there were a number of lawyers who were coming forward
15 who wanted to reserve rights or to express themselves, and I
16 effectively said 'This isn't the time for that.'

17 To what extent is there, either in process, a
18 formalized means to share information that will facilitate
19 these discussions, or some other process that you can share
20 with me that will moderate some of the potential for discovery
21 judicial proceedings of one sort or another relating to the
22 process of getting information from one party to another and
23 having what amounts to a completely transparent system for
24 discussing these issues?

25 MR. MARSAL: Well, the -- I can answer that in part,

1 Your Honor, that certain of the constituencies are actually
2 hired professionals and those professionals to represent them.
3 We have been meeting with those professionals periodically to
4 download information. I mean, you've got one group which wants
5 to argue substantive consolidation, so they want all the facts
6 that might help them on a substantive-consolidation argument,
7 and you've got another group that's separate and they want the
8 information that will help reinforce their position. We've
9 been working on that score, but that's pretty much the issue as
10 relates to today. I mean, that's pretty much where the
11 advisors are honing in on.

12 As to a process, we are actively in discussions with
13 the subcommittees representing LBT, LBSF and LBHI. And there's
14 no shortage of input, trust me on that score. And -- but what
15 we've tried to do is, again, we've tried to meet with these
16 people and to share information, provided they will -- they're
17 not -- we're staying away from asset values because we don't
18 see this as anything other than a pot plan. If you want to
19 know about asset values, then you could run amuck of maybe
20 you're trying to do something other than -- you know, there's
21 market implications to that, so as long as we stay away from
22 the assets side and focus on the claims side, we're pretty open
23 with people trying to explain to them where the negotiations
24 are.

25 Other than that, Your Honor, there's nothing more

1 formal, I mean, other than being responsive.

2 THE COURT: Mr. Miller, do --

3 MR. MILLER: Your Honor --

4 THE COURT: -- do you wish to comment?

5 MR. MILLER: If I may inter -- responding specifically
6 to your question, which arose at another omnibus hearing, in
7 connection -- there is no formal process, but there have been
8 NDA agreements entered into with most of these ad hoc
9 alliances, committees or whatever they call themselves.

10 THE COURT: Groups.

11 MR. MILLER: Groups. Anything to get away from 2019.

12 Part of the problem, Your Honor, is that most people
13 don't want to be restricted. So the process -- the formal
14 process is that those groups can hire a financial advisor and
15 investment banker, and the investment banker or financial
16 advisor has access to the material. And that process is going
17 forward. There are regular meetings. Information is being
18 distributed. A data room has been created. There is a
19 constant stream of information going into the data room, and
20 that's available to these groups that have entered into NDA
21 agreements.

22 So, responding to Your Honor's comments at the last
23 hearing, there have been tremendous efforts in that respect.
24 And so far, Your Honor, we basically have not heard any
25 complaints.

1 THE COURT: Good. I'm sure if there are complaints,
2 I'll hear about that.

3 MR. MARSAL: That's all I have, Your Honor.

4 THE COURT: Well --

5 MR. MARSAL: Do you have any questions?

6 THE COURT: -- that's quite a lot.

7 I want to express my appreciation for a very
8 comprehensive report which I find very helpful, and I hope
9 other parties-in-interest find it as helpful as I have found
10 this. I won't hold you to another one of these presentations
11 in terms of scheduling a date for one, but to the extent that
12 there are major developments in the case that in your judgment
13 you think should be reported in a public fashion, these omnibus
14 hearings represent a natural opportunity for public
15 information-sharing, and it's very obvious in the number of
16 people here that this is a subject of great public interest.
17 So, thank you very much.

18 MR. MARSAL: Thank you.

19 THE COURT: I think I'm going to take this occasion to
20 just give people who wish to go about their business elsewhere
21 and leave the bankruptcy court, either in the courtroom
22 upstairs or in this courtroom, and who have no need to stay or
23 no desire to stay to hear the remainder of this morning's
24 omnibus hearing, to leave. And what we're going to do is take
25 about a five-minute recess to allow people to reposition

1 themselves, and we'll resume in about just five minutes. So
2 we're adjourned for five.

3 MR. MILLER: Thank you, Your Honor.

4 (Recess from 10:50 a.m. until 11:02 a.m.)

5 THE COURT: Please be seated.

6 Mr. Miller.

7 MR. MILLER: Good morning again, Your Honor.

8 Returning now, Your Honor, to the agenda for the omnibus
9 hearing scheduled for today, there are two uncontested matters
10 on the agenda, Your Honor: One, number 2, is the debtors'
11 motion for authorization to reject certain executory contracts.
12 There are no objections to that motion, Your Honor. It's on
13 the calendar because the form of order has been revised
14 slightly to add a provision that claims must be filed within
15 thirty days after the date of rejection, or in such agreed time
16 as the debtors may agree to. That's the only change, Your
17 Honor.

18 THE COURT: That's fine. I took a look at the motion.
19 It seems --

20 MR. MILLER: The second --

21 THE COURT: -- routine.

22 MR. MILLER: -- item on the uncontested motions, Your
23 Honor, is the motion of Taipei Fubon Commercial Bank, Ltd. I
24 believe Morrison & Foerster represents the bank, Your Honor.

25 MS. MOLISON: Good morning, Your Honor. Stacy Molison

1 from Morrison & Foerster, on behalf of Taipei Fubon.

2 Your Honor, this is a motion to remove a consent-to-
3 transfer provision from within a loan document. There have
4 been no objections to the motion, and the relief requested is
5 similar to that that the Court granted to another lender in
6 April 2010.

7 THE COURT: Is it really removing the provision, or
8 it's simply giving the ability to transfer notwithstanding the
9 provision?

10 MS. MOLISON: The latter, Your Honor.

11 THE COURT: Okay. You can --

12 MS. MOLISON: In March 2005, Taipei Fu --

13 THE COURT: It's unopposed, and the relief is granted.

14 MS. MOLISON: Okay. Thank you, Your Honor. I have a
15 form of order.

16 THE COURT: Why don't you --

17 MS. MOLISON: Can I hand it up?

18 THE COURT: Why don't you collect it with the other
19 forms of order to be submitted today through debtors' counsel,
20 and it can be submitted at the end of the hearing.

21 MS. MOLISON: Okay. May I be excused?

22 THE COURT: You may.

23 MS. MOLISON: Thank you, Your Honor.

24 MR. PEREZ: Good morning, Your Honor. Alfredo Perez
25 on behalf of the debtors.

1 Your Honor, the next two matters on the agenda are the
2 bank settlement motions, one with Aurora and one with
3 Woodlands. We did receive several objections, comment, and
4 we've made some further modifications to the form of order. We
5 only received one objection, Mr. Kuntz, who is here in the
6 courtroom.

7 But if I could go through the presentation. We did
8 file a form of declaration for Mr. Lambert.

9 THE COURT: I read that declaration.

10 MR. PEREZ: Okay. And so, Your Honor, if I could kind
11 of go through the motion, deal with the things that we've
12 agreed on, and then Mr. Kuntz will be the only remaining
13 objecting party.

14 In essence, Your Honor, by these two motions, we
15 finally get to the point where we're having a global settlement
16 with respect to the issues that have really plagued the case
17 since the very beginning, and that is the obligations that LBHI
18 and the Lehman debtors had with respect to these two banks; one
19 is a savings bank and the other one is what is called a loan
20 production bank, Woodlands Bank.

21 We were first here, Your Honor, in February of '09,
22 and since that time we have put in substantial funds, and
23 continue to put in substantial funds. Attached to Mr.
24 Lambert's declaration was a list of all the contributions which
25 we either had made or which we had -- which we intend to make

1 by means of this motion in order to support the banks to allow
2 them to, in essence, with respect to Aurora, continue to
3 operate in the ordinary course of business so it can be sold
4 and, with respect to Woodlands, also continue to operate so
5 that it can either be sold or liquidated.

6 Your Honor, the matters involving the banks and the
7 fact that they were so intertwined with all the Lehman debtors
8 is very complex. We attached to the motion all of the various
9 proofs of claim that had been filed. There are numerous,
10 numerous claims by various Lehman entities that had claims
11 against the banks. And in addition to that, Your Honor, there
12 were the very substantial 2.2 billion dollar claims filed both
13 by the OTS and by Aurora against LBHI on account of their --
14 the master forward agreement, which the OTS takes the position
15 is in essence a capital maintenance guarantee, Your Honor.

16 Both of these banks -- both of these cases, Your
17 Honor, if you looked at the banks separately, they would
18 constitute among the largest bankruptcy cases in the country,
19 with assets almost totaling eight or nine billion dollars. So
20 these are very substantial entities. And this resolution has
21 taken a long time. I think the last -- maybe not the last
22 time, but maybe two times ago when I was here, I thought we
23 were going to be here on this final resolution a lot sooner
24 than we have been. But it's just taken a long time as a result
25 of this very, very extensive process to resolve all of these

1 things.

2 Your Honor, both proposals have been submitted to the
3 appropriate regulatory agencies: the OTS as it relates to
4 Aurora; the FDIC as it relates to Woodlands. And obviously the
5 FDIC also has some input on Aurora because it is the insurance
6 company that would guarantee it. And the applications were
7 submitted in December of last year. To our knowledge, those
8 applications are -- we've done all the work that is needed in
9 order for them to approve the applications. We've made
10 changes, at their request, to the applications and to the
11 business plans and how we would conduct the business for the
12 next eighteen months.

13 The -- based on our understanding, the Federal Home
14 Loan Bank has to determine -- I'm sorry, the Federal Reserve
15 has to determine whether these transactions constitute an
16 affiliate transaction under 13A. They either will need to
17 grant a waiver or say that they're excluded from that. And to
18 our knowledge, that seems to be the one issue that still needs
19 to be resolved so that the transactions can proceed. But I
20 think having them approved by this Court will make that
21 determination go quicker. But as far as our primary regulators
22 are concerned, to our knowledge there's nothing additional that
23 we need to do in order for the final approval to be granted.

24 THE COURT: Do the regulators know about this hearing?
25 I mean, it's obviously very public. Have they taken a position

1 with respect to this hearing? Do you have any knowledge
2 concerning their timetable? Because part of what seems to be
3 going on here is a setting of the table so that they can have
4 no excuses for not acting.

5 MR. PEREZ: Correct, Your Honor. To our knowledge, as
6 it relates to our primary regulators, which are the OTS and the
7 FDIC, we do not believe that there's anything left for us to do
8 in order for them to act. And we've addressed all their
9 concerns. We've addressed -- we've made modifications to the
10 applications. To our knowledge, we've done everything that we
11 need to do for them to act --

12 THE COURT: But effectiveness is really not about what
13 I do; it's about what they ultimately approve.

14 MR. PEREZ: Correct, Your Honor.

15 THE COURT: Okay.

16 MR. PEREZ: Correct, Your Honor. Your Honor, there
17 are various intercreditor issues implicated by the banks. And
18 during the last two weeks, we've spent a tremendous amount of
19 time with the ad hocs, with -- and with White & Case and their
20 financial advisor, as well as some of the ad hocs, going
21 through what are clearly interdebtor issues related to the
22 banks and the way that they operated.

23 We have amended the form of order to address really a
24 full reservation of rights not only as to each of the debtors,
25 whatever claims they may have, but also a full reservation of

1 rights as to the allocation of the cost and the benefits that
2 are being derived from the settlement. And at some point in
3 the future, obviously we either have to come to an agreement on
4 that or we're going to be back before the Court. But vis-a-vis
5 the banks and vis-a-vis the regulators, this is a full and
6 final settlement. It's really the -- only the intercreditor --
7 I'm sorry, the interdebtor issues that are being preserved, and
8 they're being fully preserved.

9 And I was chided the other day for perhaps being
10 imprecise at one of the hearings, talking about the fact that,
11 you know, a certain debtor was the only one that had a benefit
12 and entitlement to it. As the Court is aware, most of the
13 motions that I've been bringing up in the last several months
14 have involved situations where there have been questions about
15 the various rights as between the various debtors. So to the
16 extent that I might have said something at a hearing which is
17 not reflective of a full reservation of rights that you may
18 have in the orders, obviously the orders are what controls.
19 And I wasn't intending to affect or change the orders. I told
20 them I'd put that on the record, but --

21 THE COURT: Well, I can't tell you from memory which
22 one you're talking of. Was this Sun and Moon?

23 MR. PEREZ: It was Sun and Moon, yes, Your Honor.

24 THE COURT: Okay. Then I guess I can do it from
25 memory.

1 MR. PEREZ: Yeah, you do remember.

2 And there was -- and actually it was in that hearing;
3 it was both Sun and Moon and Innkeepers, Your Honor. But the
4 orders do reflect a full reservation of rights.

5 With that, Your Honor, unless the Court has any
6 questions about the deal -- I think the deal's been in front of
7 the Court for a long time, and it was reflected in the plan of
8 reorganization that we filed that this -- that the amounts
9 would have been contributed.

10 With that, Your Honor, let me try to address the
11 objections, and then --

12 THE COURT: Before you get to the objections, I assume
13 that you're relying on the declaration --

14 MR. PEREZ: Absolutely, Your Honor.

15 THE COURT: -- of Mr. Lambert?

16 MR. PEREZ: We're relying on the declaration to put
17 forth the business reason for our entry into the --

18 THE COURT: Is there any objection to my receipt of
19 that declaration as a proffer of what Mr. Lambert would say if
20 called as a witness in support of this?

21 (No response)

22 THE COURT: There's no objection. I accept the
23 declaration.

24 (Declaration of Douglas Lambert was hereby received into
25 evidence, in lieu of direct testimony, as a Debtors' exhibit,

1 as of this date.)

2 THE COURT: And I may have a question of Mr. Lambert,
3 in particular as it relates to Exhibit A.

4 MR. PEREZ: Yes, Your Honor.

5 Your Honor, the first objection that we received was
6 from Clayton Services. Clayton Services basically filed a
7 statement reserving their rights. They are -- there is a
8 potential avoidance action against them, and the debtors, by
9 means of my statement, confirmed that nothing in the motion or
10 order affects the rights or defenses that Clayton may have with
11 respect to the avoidance action that could be commenced by the
12 debtor, including any rights or claims that Clayton may have
13 against Aurora in connection therewith, and that all of the
14 debtors' rights and defenses, Aurora's rights and defenses, and
15 Clayton's rights and defenses with respect to that -- any
16 potential action, are reserved. So nothing in this motion and
17 order is intended to affect any situation with Clayton
18 Services.

19 Your Honor, secondly, we did receive a pleading from
20 Freddie Mac. We have made some changes in the order, which I
21 will hand the Court. But to reflect basically -- and I also
22 have a statement to read into the record. But basically
23 Freddie Mac and Fannie Mae are government-sponsored entities.
24 Ginnie Mae is a government corporation as opposed to a
25 government-sponsored entity. They all have contractual rights

1 vis-a-vis approval of the transfer of the master servicing
2 rights. And by means of this motion, as we stated in there,
3 we're going to seek their consent in order to do that. And
4 they have -- as being, you know, government-sponsored or in the
5 sense of government corporation, they have those rights.

6 So by means of this motion, we're not affecting --
7 we're not trying to affect their rights, their consent rights,
8 and by means of this motion, likewise we're not affecting their
9 rights generally that they may have pursuant to their
10 contracts. So, in essence, neither the motion nor the order
11 affect those rights.

12 So with respect to Freddie Mac, LBHI owns a portfolio
13 of mortgage servicing rights with respect to certain Freddie
14 Mac and Fannie Mae sponsored residential mortgages. LBHI
15 appointed Aurora (sic) Services, LLC, or ALS, as a subservicer
16 of those loans, and the servicing is currently being provided
17 by ALS. Pursuant to the settlement agreement, LBHI proposes to
18 transfer such mortgage servicing rights to FSB, subject to
19 Freddie Mac and Fannie Mae -- and Fannie Mae is in
20 conservatorship -- and their conservators' consent.

21 Now, LBHI agrees that it will not, without such
22 consent, transfer to Freddie Mac and Fannie Mae mortgage
23 servicing rights to Aurora or Aurora Loan Services or their
24 affiliates, or assign the income receivable or -- received or
25 receivable by LBHI that is attributable to or derived from such

1 servicing to the FSB or Aurora Services or any such affiliate
2 entity for a period of 120 days or such period as may be
3 extended by the parties so that the parties can try to obtain
4 the consent of Freddie Mac, Fannie Mae and their conservator
5 for the transfer of such servicing rights to the FSB or Aurora
6 Services. And the parties reserve all their rights with
7 respect to such transfer of the mortgage servicing rights or
8 any income in connection therewith, in the event that any
9 agreement in respect to such consent is not reached. And
10 nothing herein constitutes a waiver of any of Freddie Mac's,
11 Fannie Mae's or their conservators' rights or claims regarding
12 the subject residential mortgage loans, or constitute a waiver
13 of any of the conservators' rights under the Federal Housing
14 Enterprises (sic) Safety and Soundness Act of 1992 as amended
15 by the Housing and Economic Recovery Act, Public Law 110-289.

16 Your Honor, I believe, with that statement in the
17 record as well as the change that we've made to the order, that
18 the concerns raised by Freddie Mac are obviated.

19 THE COURT: Is there anyone here acting on behalf of
20 Freddie Mac who can confirm that the statements just read into
21 the record will be sufficient for these purposes?

22 MS. REE: Good morning, Your Honor. Sophia Ree from
23 Landman Corsi Ballaine & Ford, on behalf of Freddie Mac.

24 Based on what was read into the record, Freddie Mac
25 has no objections, Your Honor.

1 THE COURT: Fine. Thank you.

2 MR. PEREZ: And, Your Honor, I believe that Ginnie
3 Mae, who's represented by the U.S. Attorney -- we have agreed
4 to insert -- the way we had drafted the order, we talked about
5 government-sponsored entities that had this full reservation.
6 There is a concern about including Ginnie Mae as one of the
7 government-sponsored entities. So we've just flipped the
8 order. Unfortunately it's -- I have it handwritten, but we've
9 just flipped the order. So we put Ginnie Mae and the
10 government-sponsored entities Freddie Mac and Fannie Mae. But
11 the same reservation and the same comments that I've made with
12 respect to Ginnie Mae and Freddie Mac also -- I'm sorry, Fannie
13 Mae and Freddie Mac, also apply to Ginnie Mac. And I believe
14 counsel also has a statement, and I think, with that, that
15 resolves their concern.

16 MR. CORDARO: Thank you, Mr. Perez.

17 Good morning, Your Honor. Joseph Cordaro, Assistant
18 United States Attorney, on behalf of Ginnie Mae. And, yes,
19 that -- there is an issue. Ginnie Mae technically is not a
20 GSE. It's a government corporation. Hence, the change, that
21 Mr. Perez just mentioned to Your Honor, to the order. And just
22 to confirm what I believe Mr. Perez told Your Honor, that
23 there's nothing in the motion, or the order granting the
24 motion, that modifies or restricts any rights of Ginnie Mae
25 under any agreement with either the debtors or Aurora Bank FSB.

1 And we come to that agreement; I believe Mr. Perez articulated
2 it. So --

3 THE COURT: Understood.

4 MR. CORDARO: Thank you, Your Honor.

5 MR. PEREZ: Your Honor, next we come to the statement
6 filed by the ad hocs. I think that I've addressed it. The --
7 we have, at their request, gone back and done -- and are doing
8 basically further due diligence on some of the issues that
9 they're concerned -- that process is continuing and we will
10 finalize that process before the closing takes place; it's just
11 a matter of getting the documents. The debtor and its counsel
12 who's handling this feel very comfortable that the issues --
13 first of all, that they've already looked at the issues raised,
14 and that is any potentially contingent liability that you might
15 be creating by the transfer of the servicing rights; feel that
16 that issue is -- doesn't exist, and they're going back again
17 and confirming to themselves that -- again, they confirmed that
18 the issue doesn't exist.

19 And we did make --

20 THE COURT: I'm confused. I'm sorry to break in, Mr.
21 Perez. I'm confused by what you just said. Is there a
22 condition subsequent that needs to be satisfied --

23 MR. PEREZ: Your Honor --

24 THE COURT: -- in order to make the objection of the
25 ad hoc committee go away?

1 MR. PEREZ: No, Your Honor, I don't believe that it's
2 a condition subsequent. We are endeavoring and think that --
3 as a result of the fact that we're going to have a little bit
4 of time before we have final regulatory approval, to finish the
5 work that we started again last week. But we've committed to
6 do that and report to them before we close or report to them
7 where we are when we're going to close.

8 THE COURT: And this is the group represented by Mr.
9 Uzzi?

10 MR. PEREZ: Excuse me?

11 THE COURT: This is the group represented by Mr. Uzzi?

12 MR. PEREZ: Yes.

13 THE COURT: I'd like to hear from him. Well, I'm
14 going to hear from his partner, from Mr. Shore.

15 I just want to understand the status of your objection
16 at this point.

17 MR. SHORE: Sure. And I can either address -- I had a
18 couple of statements to make on the record today with respect
19 to both the motions, and I can table them for now. But with
20 respect to the specific question, there's no condition
21 subsequent. We trust that the debtors, having done the due
22 diligence, if they find something in there that would require
23 them to reassess the motion or going forward with the
24 transaction, they're perfectly capable of pulling the plug on
25 that transaction, because they're only seeking authorization

1 and not a direction to do it. But as long as we understand
2 that they are going through that process, we have no objection.

3 THE COURT: Okay. Thank you.

4 MR. PEREZ: So, Your Honor, I think that that
5 addresses all of the objections, other than the one filed by
6 Mr. Kuntz.

7 THE COURT: Mr. Kuntz, do you wish to speak?

8 MR. KUNTZ: Thank you, Your Honor. First I'd like to
9 clarify one thing. I believe Mr. Miller spoke this morning
10 earlier and he referred to Washington Mutual in relationship to
11 Wachovia. I believe Washington Mutual was acquired by
12 JPMorgan. And Wachovia was acquired by Wells Fargo. I know
13 this only because I was a -- I had my credit card with
14 Washington Mutual.

15 What concerns me here is the use of additional estate
16 funds versus estate assets. And yesterday afternoon I filed,
17 in accordance with Your Honor's prior comment, a notice to call
18 the deponent to the stand, and I've already provided a punch
19 list of perhaps fifteen questions, because I really don't think
20 that they've done their homework, they've expanded all the
21 options that are available. It's just simply the government
22 wants the money, here, we'll give them two billion to keep them
23 happy. For instance, I put in 'What about the Park Avenue
24 mortgage?' From my understanding, that Park Avenue mortgage
25 could be transferred to these banks. They could then take that

1 mortgage and go to the Federal Reserve, Federal Home Loan
2 Savings Bank, and get 6-, 7-, 8-, 900 hundred million dollars
3 in cash.

4 As I put in my prior papers, these are run-of-the-mill
5 institutions. There's nothing special about them that requires
6 a billion more of cash put up to keep them in a situation in a
7 world where the business model of lending money doesn't really
8 exist anymore. I mean, just yesterday I read that General
9 Motors Acceptance Corp. has suspended filing all foreclosures
10 in the entire country. So what's going to happen to Woodlands
11 and what's going to happen to Aurora if all of a sudden there's
12 another billion, here's another billion? Whoops, all your
13 mortgages now are suspended for two years. If the
14 administration comes out and says 'We have a crisis. Guess
15 what, guys? Your mortgages are now suspended,' what's going to
16 happen to the cash flow?

17 THE COURT: Is your objection, Mr. Kuntz, that you
18 question the business judgment of the debtors in proposing to
19 satisfy some of the regulatory problems impacting these two
20 institutions by investing capital into these assets for a
21 future sale or disposition?

22 MR. KUNTZ: Cash.

23 THE COURT: Is that -- did I --

24 MR. KUNTZ: Not assets.

25 THE COURT: Did I correctly summarize what is your

1 objection?

2 MR. KUNTZ: Cash, not assets. And I have -- I'd like
3 to call the witness to the stand and ask him. I said have
4 you -- I filed a notice, Your Honor, yesterday, as you
5 instructed previously that 'If you want to call the witness to
6 the stand, you have to file with the Local Rule,' which I did.

7 THE COURT: Okay, so you want to examine Mr. Lambert,
8 is that right?

9 MR. KUNTZ: Yes, sir. Yes, Your Honor.

10 THE COURT: Mr. Lambert is here.

11 MR. KUNTZ: And I would like that the record reflect
12 that yesterday I went to mail copies of the time-stamped
13 documents, and the mailing standards from the Whitehall Post
14 Office wouldn't accept them. So I have a copy for the debtors'
15 counsel --

16 THE COURT: What is it you're handing to Mr. Miller?

17 MR. KUNTZ: It's the time-stamped copy of the notice
18 to call the deponent to the stand.

19 THE COURT: Okay.

20 Is there any objection to having Mr. Lambert appear as
21 a witness?

22 MR. MILLER: No, Your Honor.

23 THE COURT: Fine.

24 Mr. Lambert, why don't you come forward? Yeah, come
25 to the stand.

1 And before questions are asked by Mr. Kuntz, I had
2 some questions that I noted I wanted to ask Mr. Lambert, so I'm
3 going to ask those questions first.

4 MR. KUNTZ: I understand, Your Honor, but I just --
5 can I provide a copy -- I have the questions here. Could I
6 provide a copy of -- to Mr. Lambert, or counsel can also?

7 THE COURT: Well, ordinarily you would just ask them.

8 MR. KUNTZ: Well, I understand, but these are, like --
9 I didn't want to attack them by surprise. And also one other
10 thing: In the interest of judicial economy, as Your Honor is
11 aware, my standing has been challenged now finally, and there
12 were three minor matters which I withdrew my objections to.
13 But this is such a large number, I felt that I should at least
14 make my objection known. I mean, a billion dollars --

15 THE COURT: Well, why don't you --

16 MR. KUNTZ: -- in fees --

17 THE COURT: -- why don't you --

18 MR. KUNTZ: -- have been paid --

19 THE COURT: -- sit down for a moment --

20 MR. KUNTZ: Thank you, Your Honor.

21 THE COURT: -- and I'm just going to ask Mr. Lambert a
22 couple of questions that I had.

23 But, first, since you're here -- you've spoken to the
24 Court before from the podium. I'm going to swear you as a
25 witness. Please stand up and raise your right hand.

1 (Witness sworn)

2 THE COURT: Be seated please. Mr. Lambert, I took a
3 look at your declaration, which is now in evidence, and I just
4 am interested in the cost benefit analysis that's attached to
5 your declaration in particular. And I'm looking for -- in
6 effect, more detail --

7 THE WITNESS: Sure.

8 THE COURT: -- if you can provide it.

9 THE WITNESS: I'll try.

10 THE COURT: My best recollection from what I saw is
11 that you estimate approximately a three billion dollar overall
12 advantage to the estate by virtue of these transactions, and
13 I'd like to understand, since it's a very spare cost benefit
14 analysis, what assumptions were made in order to reach that
15 conclusion --

16 THE WITNESS: Sure.

17 THE COURT: -- and to understand something more about
18 your analysis.

19 THE WITNESS: As you know, back in probably fourth
20 quarter of '08 and the early days of the first quarter of '09,
21 we had many discussions with Debtors' counsel, counsel to the
22 UCC, regulatory counsel, and expressed to the Court, I think,
23 in a presentation that Mr. Marsal made in February of '09, the
24 risk to the estate of the regulators bringing a 365(o) claim
25 against the estate. And at that time, I believe we estimated

1 that potential exposure to be approximately 2.7 billion, I
2 think, at the time.

3 We -- and that obviously had weighed on many of the
4 decisions that we've made since the commencement of this case.
5 Again, while I think we've always felt -- or the debtor, as
6 well as the banks, have felt that there were adequate defenses
7 against that claim, certainly there was a concern that, if
8 brought by the federal government, they could be successful,
9 and the detriment to the estate would be significant.

10 The analysis that I attached to my declaration assumes
11 today that we will be -- the estate and/or various debtors of
12 the estate will be receiving back various pledged collateral
13 that was pledged to both banks. And, again, we look at the
14 assumed current value of that collateral coming back. Further,
15 as I think we've presented in the plan of reorganization and
16 disclosure statement, we believe that, in the case of
17 Woodlands, it is most likely that we will liquidate that
18 institution in place and ultimately surrender the charter for
19 that industrial lending corp. -- bank. And with respect to
20 Aurora Bank, we believe that it is most likely that that
21 institution will be sold to a third party in order to maximize
22 value and recovery to the estate.

23 So when taking together either the liquidation through
24 liquidation in place or sale proceeds of the two institutions,
25 together with the value of the collateral coming back, I think

1 we reasonably expect that value to be approximately two billion
2 dollars today; and, you know, potentially some further upside
3 to those numbers.

4 We look at, again, the avoidance of the loss to the
5 estate of approximately -- 2.7 billion, I believe, is the
6 number; I don't have the schedule right in front of me -- which
7 suggests a value and/or claims avoided, aggregating 4.7
8 billion. Assuming that the motions that are before the Court
9 today are approved and the estates go forward with making the
10 final contributions, we believe, in the aggregate on a gross
11 basis, we will have contributed cash, other assets, as well as
12 the cancellation of indebtedness, to the tune of 1.6 billion to
13 both institutions, which suggests to us -- and we believe
14 that -- you know, it was a conclusion that we had in early '09
15 and it's the same conclusion that we draw today that we will
16 have saved or preserved value to the estate of approximately,
17 you know, 3.1 billion dollars by the actions that have been
18 taken to date as well as if we take action pursuant to the
19 motions before the Court, if that answers your question.

20 THE COURT: Yeah, so the essence of this is that
21 there's an avoided substantial claim of 2.7 billion dollars and
22 a realization as a result of disposition --

23 THE WITNESS: Correct.

24 THE COURT: -- of underlying assets that, on a net
25 basis, you estimate is about 3.1 billion dollars to the benefit

1 of the estate?

2 THE WITNESS: That is correct.

3 THE COURT: Okay. Thank you.

4 THE WITNESS: You're welcome.

5 THE COURT: Mr. Kuntz, if you have questions, this is
6 the time.

7 MR. KUNTZ: Thank you, Your Honor.

8 CROSS-EXAMINATION

9 BY MR. KUNTZ:

10 Q. Good morning, Mr. Lambert.

11 A. Good morning.

12 Q. Have you worked for a bank?

13 A. I have.

14 Q. Which bank?

15 A. National Bank of North America.

16 Q. Are you an officer of either Aurora or Woodlands?

17 A. No, I'm not.

18 Q. Are you a director of either Aurora or Woodlands?

19 A. I'm a director of both institutions.

20 Q. When the settlement was proposed with JPMorgan, was any
21 part of the Woodlands or Aurora alleged equity considered as
22 part of or in place of the 500 million in cash paid to
23 JPMorgan?

24 A. I'm not sure I understand your question or the
25 connectivity between the CDA with JPMorgan and the banks.

1 Q. There was a settlement previously approved by this Court.
2 As part of that settlement, the debtor gave JPMorgan 500
3 million in cash.

4 A. Correct.

5 Q. Was it ever considered to give part of the Woodlands or
6 Aurora equity to JPMorgan in place of the cash?

7 A. I was not involved with those negotiations, but I would
8 suspect that JPMorgan was looking for liquid assets, cash, in
9 connection with that transaction. So I'm not sure that anybody
10 considered turning over equity value of either institution to
11 JPMorgan.

12 Q. Has a spinoff of Aurora or Woodlands to Lehman creditors
13 been considered?

14 A. That is a potential option in the disposition of one or
15 both banks.

16 Q. What effect would the transfer of the Park Avenue
17 mortgages have on the Aurora or Woodlands balance sheet?

18 MR. PEREZ: Objection, Your Honor. Irrelevant.

19 THE COURT: I don't understand the question either.

20 MR. KUNTZ: Thank you.

21 Q. The debtor has, it's my understanding, almost a billion
22 dollars in mortgages on the, I think, 237 Park Avenue building.

23 THE COURT: Well --

24 Q. If --

25 THE COURT: -- I sustain the objection. It's not --

1 it's conflating one asset with the need to cure some regulatory
2 problems affecting other assets. And it's really an
3 inappropriate question, so I sustain the objection.

4 MR. KUNTZ: Then I'll skip to the next three.

5 Q. Was there ever any consideration of transferring the
6 junior mortgage on the Hancock Center to Aurora or Woodlands?

7 MR. PEREZ: Same objection, Your Honor.

8 THE COURT: Same ruling, and --

9 MR. KUNTZ: Thank you, Your Honor.

10 THE COURT: -- the objection is sustained.

11 Q. Has there ever been a consideration of transferring the
12 empty building in Stamford, Connecticut to Woodlands or Aurora
13 to bolster the balance sheet?

14 MR. PEREZ: Same objection, Your Honor.

15 THE COURT: And same ruling.

16 I mean, Mr. Kuntz, I understand what you're getting
17 at, but --

18 MR. KUNTZ: Your Honor, I take the objection. I'll
19 just simply finish my questions and I'll be done. Thank you.

20 THE COURT: Okay.

21 Q. How much ground rent is being paid to General Re, if you
22 know?

23 A. I do not know.

24 Q. Are you aware that the allowed claims in the Stamford,
25 Connecticut building have been acquired by Barclays?

1 MR. PEREZ: Same -- could I just have a running
2 objection on relevancy, Your Honor, so I don't have --

3 MR. KUNTZ: I believe this goes to the
4 business-judgment rule, Your Honor. If --

5 THE COURT: Well, without limiting your ability to ask
6 questions, the questions do need to relate to the substance of
7 the motion that's before the Court. And the motion that's
8 before the Court is very specific; it's a series of settlements
9 that are designed to cure certain regulatory problems that have
10 plagued Woodlands and Aurora from the very beginning of these
11 bankruptcy cases.

12 MR. KUNTZ: I understand, Your Honor, and --

13 THE COURT: And you're talking about a series of
14 other assets and transactions.

15 MR. KUNTZ: Mr. Lambert is a senior member of the
16 debtors' management, and they continue to roll out this
17 business-judgment rule, and I'm simply asking questions. For
18 instance, it seems to me that if the Court approved and allowed
19 claims to Bank of America, a/k/a Security Pacific, and then
20 Barclays acquired that claim and now Barclays is being sued
21 by -- for I don't know how much money, that this would be
22 something senior management would be aware of. I was shocked
23 when I read that.

24 THE COURT: Well, your questions for today need to
25 relate to the subject matter of the motion that's before the

1 Court.

2 MR. KUNTZ: Well, then I'll -- let me skip down.

3 BY MR. KUNTZ:

4 Q. Has there ever been a consideration of transferring the
5 Sun and Moon property to Woodlands or Aurora to bolster the
6 balance sheet?

7 A. Well --

8 MR. KUNTZ: Same objection?

9 Q. Has the concept of investing one billion dollars in
10 Citibank stock, together with a transfer of Aurora or Woodlands
11 to Citi, ever been considered?

12 A. Are you -- could you restate the question? I'm sorry, I'm
13 not sure I understand.

14 Q. Has the concept of investing the one-billion-dollars-plus
15 that's proposed to be put into Woodlands or Aurora -- has a
16 consideration been made of buying Citibank stock and then, in
17 essence, transferring the Woodlands/Aurora problems to
18 Citibank?

19 A. I'm not sure I understand how buying stock of another
20 regulated institution would in turn transfer
21 liability/obligation to Citibank.

22 Q. If Citibank acquired these two institutions, then the big
23 bad government claim would go away, as I understand it.

24 MR. PEREZ: Your Honor, I'm going to object again.
25 Relevancy.

1 THE COURT: Well, I think you could also object to the
2 fact that it's not a question. It was just a statement of Mr.
3 Kuntz. It's sustained.

4 MR. KUNTZ: Well, at this point, Your Honor, I can see
5 that, you know, the Court really doesn't want to hear what's
6 really going on in the debtors' minds, and --

7 THE COURT: No, what I want to hear, and I'm giving
8 you the opportunity to do it, are questions that relate to the
9 motion.

10 MR. KUNTZ: Yes, and the questions relate to the
11 business-judgment rule behind putting another billion
12 dollars --

13 THE COURT: That would mean --

14 MR. KUNTZ: -- of cash --

15 THE COURT: That would mean that you would have to ask
16 questions about these institutions, about their capital
17 adequacy --

18 MR. KUNTZ: Yes, that's why --

19 THE COURT: -- about the kinds of claims that the
20 government might make under 365(o), whether or not those claims
21 are in fact hundred-cent-dollar claims.

22 MR. KUNTZ: I'm not --

23 THE COURT: Those would be real relevant questions.
24 You haven't asked those questions.

25 MR. KUNTZ: The question, Your Honor, as I understand

1 it, is the inadequacy of the balance sheet of the subject
2 banks. And if a billion-dollar mortgage was transferred, not
3 cash, mortgage was transferred to these banks, and the banks
4 could go to the Federal Reserve or whoever and borrow against
5 that collateral, then it seems to me that that would solve the
6 accounting question that the government has.

7 And by the way, we are here because the federal
8 government, as Mr. Miller said, left Lehman out in the cold.
9 Right? At this point, Your Honor, I'll just leave it at that.
10 I don't have any more to say.

11 THE COURT: Okay.

12 Is there any --

13 MR. PEREZ: I have nothing further, Your Honor.

14 THE COURT: -- any examination of the witness?

15 MR. PEREZ: I don't have any questions for Mr.
16 Lambert.

17 THE COURT: Okay.

18 Mr. Lambert, thank you.

19 THE WITNESS: Thank you.

20 THE COURT: You're excused.

21 (Witness excused)

22 MR. PEREZ: Your Honor, by way of argument, I wanted
23 to highlight a couple of things. Number one, we did start this
24 process back in February of '09, trying to address -- at the
25 time, you know, there was a very material chance that these

1 banks would be seized. And we have put in substantial amounts
2 of money, culminating in the 477 million dollars that we
3 propose to put in by means of this motion.

4 I do want to highlight the fact that, as against
5 Aurora, the -- I'm sorry, by Aurora, on account of Aurora,
6 there is a 2.2 billion dollar claim asserted by the bank.
7 There's a 2.2 billion dollar claim -- there are two 2.2 billion
8 dollar claims asserted by the OTS. Those claims, one of which
9 is on account of 365(o), which would result -- if that claim
10 was found to be valid, would result in a 507(a)(9) priority.
11 So those would be one-hundred-cent dollars that would have to
12 be paid, same as if it were a fully secured claim. In
13 addition, Your Honor, there is a 23(a) claim as a result of a
14 concern about an affiliate transaction.

15 We did attach to the motion all the various claims
16 that were filed against the entities, against Woodlands, which
17 total in excess of a billion dollars. And after you reduce
18 them for duplicates, it's something less than that. But they
19 are very significant.

20 This is a very difficult situation. This was not a
21 situation that -- this has been one of the more difficult
22 situations that the bank has faced -- I'm sorry, that Lehman
23 has faced, for two reasons. First of all, we've had a very
24 volatile environment. And these banks, when they were char --
25 when they were purchased by Lehman, went on mark-to-market

1 accounting, which was the way Lehman accounted. And generally
2 banks don't do mark-to-market accounting because when you've
3 got a loan that's paying interest and you realize on it,
4 there's no need to mark to market as you would a securities
5 firm that has volatile securities.

6 So we had a situation where, although the assets were
7 performing as a result of the accounting principles, the fair-
8 value accounting, you ended up marking it and there was a real
9 chance that they were going to be taken, coupled with the
10 potential priority claims, coupled with the fact that, under --
11 because LBHI was a bank holding company, the FDIC, if it
12 stepped in and took one bank, was authorized by statute to take
13 the other bank. So it could have been a situation where not
14 only would we not have had any assets left because of a fire
15 sale liquidation, but there would also have been a very, very
16 significant claim that would have had priority.

17 After many, many months of trying to negotiate this,
18 Your Honor, we've come before the Court, presenting this
19 proposal which we think is the way to really maximize value and
20 avoid significant potential priority claims.

21 That's all, Your Honor.

22 THE COURT: Okay. I'd like to hear from the
23 creditors' committee because I know the committee supports the
24 transaction; I'd like to know why.

25 MR. O'DONNELL: Your Honor, Dennis O'Donnell, Milbank,

1 Tweed, Hadley & McCloy, on behalf of the official committee of
2 unsecured creditors.

3 Your Honor, as you rightly point out, we've been here
4 every time the debtors have been here for the past year and a
5 half, supporting the previous infusions and currently support
6 this final resolution. It hasn't been an easy task for the
7 committee. I mean, the committee did not start out thinking
8 that this was necessarily a good idea, and convincing the
9 committee took time and effort, working with them, working on
10 the legal issues in terms of the priority claims, and
11 working -- having our financial advisors vet everything the
12 debtors were doing in terms of the potential values here. But
13 we got there. We got there sometime ago and we've been side by
14 side with the debtors throughout this process, convinced that
15 doing what we need to do here to get over the regulatory
16 hurdles will result in value to be reaped from this investment.

17 We -- I would -- in the context -- I mean, as I say,
18 we -- it hasn't been an easy process. We know that this is a
19 lot of money. We know that this is a substantial investment,
20 has been and continues to be. We acknowledge some concerns in
21 terms of using the estates' assets with respect to an
22 investment that is not guaranteed, but there are no guaranteed
23 investments here. We believe that the debtors' business
24 judgment here in making this investment is the best viable
25 option at this point and should yield to substantial value in

1 the long term.

2 Commenting as well on Mr. Kuntz's potential
3 substitution, and I think what he was -- his questions were
4 going to were, were other -- whether -- did the estate -- did
5 the committee consider the use of other assets here instead of
6 cash for the other consideration that's being used, and the
7 answer's yes, all options were considered. I think the answer
8 with respect to the assets you were referring to, the
9 real-estate ones, is that the government did want those types
10 of assets. What they're getting -- I mean, what we ultimately
11 settled on was the type of assets, the type of contributions
12 that would be acceptable to the government. And we are where
13 we are. We have a settlement before you, and that's the issue
14 for the Court.

15 One further -- in terms of the fact that the
16 regulators have not yet approved this, that is a concern, but
17 not a great concern. We believe that there is enough momentum
18 with the regulators for this to get done in short order.
19 There's one minor hurdle, we believe, to get order, and that
20 will be done. And nothing will happen with the settlement
21 until that happens. We take comfort that this is a package
22 deal and, if it's going to get done, it's going to get done as
23 written with full approval by the regulators. And the money
24 will not get invested without that approval.

25 And finally, Your Honor, on the allocation issues,

1 which we think have been resolved, or clarified at least, I
2 think there was always an understanding that the proposed
3 allocations of the benefits and burdens in the motion were
4 subject to a reservation of rights. The order as modified does
5 in fact make it very clear that they are subject to being
6 revisited if need be. We think the allocations as proposed
7 make some sense but, with the reservation of rights, everyone
8 will have the opportunity to confirm that in the future.

9 And that's all I have to --

10 THE COURT: All right, thank you.

11 Does anyone else wish to be heard on this?

12 MR. SHORE: Chris Shore from White & Case, for the ad
13 hoc group. I've got two things I'd like to focus on, and I'll
14 try to be brief.

15 We look at the Aurora and Woodland settlement as
16 having two pieces: First there's a bank settlement piece,
17 which is the interface between the enterprise and the banks;
18 and then there's a debtor settlement, which is the interface
19 between each of the individual debtor estates and what's being
20 resolved in the motion.

21 With respect to the bank motion -- or the bank
22 settlement, that is, the interface between the debtor estates
23 and the banks, we started out very concerned about the
24 investment strategy, which is essentially a doubling-down and
25 putting in a billion dollars of new equity in order to save old

1 equity. And it's not just a 365(o) issue. Obviously that has
2 always been a concern, but be clear by this motion the debtors
3 are accepting 365(o) liability, because they've entered into
4 what is indisputably a capital maintenance agreement, which
5 is -- so if anything bad goes on from now, that issue seems to
6 be resolved.

7 It's also an issue of this is going in as equity. And
8 the issues we had and the issues the debtors are working on and
9 the questions we've been asking are what are the risks to that
10 equity investment going into the banks, versus just leaving
11 things as they are now and resolving the 365(o) liability as
12 best we can as it exists. And we've worked with the debtors
13 all last week. We had a number of calls over the weekend. The
14 process is ongoing. But I think we've gotten ourselves to a
15 fragile approval of the motion where the questions have been
16 answered or are being answered, such that the nature of a very
17 large equity investment to save old equity is something we can
18 agree with.

19 With respect to the debtors' settlements, we
20 appreciate that the statements are being made now that it
21 wasn't intended to be a final allocation. We did have concerns
22 with respect to two aspects of the motion: first, the manner
23 in which the allocation of the costs were going to be done, in
24 particular, for example, on the Woodlands side, the allocation
25 of cost based upon bank-filed claims; and also there are going

1 to be a number of interdebtor asset transfers going on.

2 Again, we've had a lot of discussions with the
3 debtors. They've given us comfort that it's not their intent
4 to resolve those finally. And I think Mr. Miller's comments
5 before are telling. He's standing up. Look, they recognize
6 the issue. We see the issue. We're trying to reserve rights
7 now.

8 So let me give you an example. There's an agreement
9 in principle disclosed in the Aurora motion that LCPI is going
10 to be purchasing Archstone loans at ninety percent of fair
11 market value. Well, that settlement really was one individual
12 acting on behalf of LBHI and LCPI, saying what is fair in this
13 context for going back and forth, and ninety percent of fair
14 market value -- our question's why not ninety-five percent --
15 I'm sure somebody else has a question why not eighty-five
16 percent -- and more importantly, what is fair market value. I
17 think if we've seen anything in this case, a lot of very
18 sophisticated people can disagree as to how to make marks on an
19 asset.

20 They may have come to the right settlement; they may
21 have not. We weren't in a position, in the time given, to come
22 up with a definitive view as to what the right allocations are.
23 But we -- so we've agreed to a reservation of rights that lets
24 the debtors proceed with a bank settlement and getting that
25 done -- again, that's an important piece of this -- and that

1 allows the debtors to close their books provisionally. They
2 have to do something with the accounting for the transaction
3 that allows it to do it, but allows any party-in-interest, as
4 part of some process at some point, to look at the bona fides
5 of this and come up with an approval.

6 I suspect, just as far as keeping the Court apprised,
7 that if the debtors go forward and transfer assets from LBHI to
8 LCPI at this ninety percent of fair market value as they're
9 calculating, we may have to come back to the Court on that. I
10 just don't think that there's an agreement, just looking at it
11 from an LBHI perspective, that that transfer at that price
12 makes sense, and we're talking about hundreds of millions of
13 dollars here.

14 I recognize, again, on behalf of the group, that these
15 kind of reservations are cumbersome from a judicial economy
16 standpoint. We'd like to wrap up all resolutions with respect
17 to one subject matter at the same time. But at this time, we
18 don't have anybody to negotiate. If the debtors recognize they
19 can't come to a final settlement and there's nobody there for
20 LCPI, there's really no way to resolve that issue without
21 coming to the Court. And we apologize for, again, the
22 reservations of rights and the need maybe to come back on that,
23 but we don't have a structure.

24 I don't want to sound like a broken record, but there
25 needs to be something in place. This is coming up consistently

1 and it's going to have to come up over time as this gets done,
2 because I'm going to clarify two things from the State of the
3 Estate address: This isn't a pot plan, per se, absent an
4 agreed settlement. When we talk about assets and liabilities,
5 distributions are going to be made out of estates, based on the
6 assets and liabilities. If there are disputes as to who owns
7 the asset or where the liability resides, or what price an
8 asset was transferred, that's all going to have to be resolved
9 at some point, and it's going to have to be resolved pursuant
10 to some process.

11 The only other thing I'd like to add as far as the
12 process as it exists today, I don't necessarily -- I guess I
13 can agree that there are no disputes that have been brought
14 before the Court on that. I don't think it's fair to say that
15 there aren't disputes. We've been asking for documents since
16 June. There has been a database set up. There are five
17 hundred and, I think, seventy as of last count, documents in
18 that database, substantially -- more than half of which are
19 public documents.

20 So I don't think -- I think we have information
21 bottlenecks now. There were issues with respect to signatures
22 of NDAs and getting people engaged. The process is started.
23 But from a disclosure standpoint, I think if that bottleneck
24 doesn't open up and that there's more population with
25 documentation, we may have to be back before the Court.

1 THE COURT: My door's always open. But to be clear,
2 Mr. Shore, because you used this occasion, and that's fine, to
3 in effect respond to some of the things that came up during the
4 State of the Estate section of this morning's hearing, but as
5 it relates to the motion that's currently before me and your
6 reservation of rights with respect particularly to allocation
7 issues, those rights having been reserved, your group having
8 examined this transaction with the perspective of -- actually
9 the same perspective as Mr. Kuntz; and not wanting to throw
10 good money after bad to preserve equity, old equity especially,
11 you're satisfied -- well, at least your group is satisfied,
12 that this is a reasonable transaction in respect of protecting
13 these banking assets?

14 MR. SHORE: Yes, we do (sic), Your Honor.

15 THE COURT: Okay. I wanted to confirm that.

16 MR. PEREZ: Your Honor, I'm not sure I have any real
17 response to Mr. Shore's comments, because they largely didn't
18 have to do with the motion, but there is one thing that I would
19 want to respond to, and that is that there was some indication
20 that there was one person who was making all of these
21 decisions. I mean, all of these decisions are made by groups
22 of professionals, the committees involved. I mean, this is not
23 something that some person dreams up by himself and wearing all
24 kinds of hats. I mean, this is -- it's done very thoughtfully,
25 with a lot of input by professionals who do this, or who are

1 trying to get to the right decision.

2 And with that, Your Honor, I don't have anything
3 further.

4 THE COURT: All right.

5 Is there anything more?

6 (No response)

7 THE COURT: This has been a problem that has been
8 presented on a number of prior occasions, namely the need to
9 provide infusions of equity to support Aurora and Woodlands and
10 to bring these institutions properly within regulatory
11 compliance. One of the problems, from the Court's perspective
12 during each one of those prior occasions, and today is no
13 exception, is that the role of the regulators has been somewhat
14 obscure. We know they're there. We know that they need to
15 take some kind of action to say yes to these various attempts
16 to bring the institutions within regulatory compliance. But
17 even today I'm being asked to approve very significant
18 transactions without knowing that the approval will lead,
19 within some demonstrated period of time, to approval by the
20 regulators themselves. In effect, as I said earlier during
21 colloquy, I'm being asked to set in motion a process such that
22 the regulators should have no reason to say no and shouldn't be
23 in a position to say 'Well, wait a minute, you don't have
24 bankruptcy court approval.' That approval will have been
25 obtained as a result of today's hearing and so, presumably,

1 that will create some momentum toward bringing this to a final
2 resolution.

3 I understand what's going on. I also understand some
4 of Mr. Kuntz's concerns as an observer. But I am satisfied
5 that the debtors are exercising well-informed business judgment
6 in an area that is not free from doubt. The fact that the
7 creditors' committee has been closely associated with this
8 process for the last eighteen months and has presumably,
9 through one of its subcommittees, been monitoring this and
10 exercising independent judgment as a watchdog, and also
11 considering the business judgment that's being proposed by the
12 debtor, is a source of comfort to me.

13 Additionally, Mr. Shore's clients represent entities
14 that have significant economic stakes in these proceedings,
15 presumably through acquired claims but that doesn't matter, and
16 they have an interest in maximizing value and preserving
17 rights. In effect, these natural economic forces that are
18 operating within the case provide some additional comfort in
19 assessing the reasonableness of the business judgment that is
20 being exercised by the debtors.

21 The only real live objection at this point is Mr.
22 Kuntz's objection, which is an objection more to the use of
23 cash as opposed to other kinds of consideration or collateral
24 or assets that might be offered up to make the regulators
25 happy. With respect to that position, I believe that the

1 debtors, the creditors' committee and those who are closely
2 monitoring this process for the banks themselves have done all
3 that they can reasonably do to try to satisfy a difficult
4 situation. Everybody involved has recognized that this is
5 difficult in part because we're dealing with regulators who are
6 not here in court, and I find that a little troublesome but I
7 can't force them to appear. It would be much more comforting
8 to me if I were being asked to approve something and I knew
9 that at the time of approval that a deal was going to be inked
10 and executed promptly thereafter. Instead, this is a little
11 bit of a black box. And it is really that aspect, as opposed
12 to Mr. Kuntz's objections, that I find most troublesome.

13 Notwithstanding that, I accept the business judgment
14 of the debtors as validated by the creditor constituencies that
15 have been monitoring this, and I approve the motion as
16 presented, both as to Aurora and Woodlands.

17 MR. PEREZ: Thank you, Your Honor. We are going to
18 need to change one of the orders to reflect the comments from
19 the U.S. Trustee. So we will submit that order later on today
20 after we get back to the office.

21 THE COURT: That's fine.

22 If there are parties who wish to be excused who were
23 involved in the Aurora and Woodlands matters, they can be
24 excused. But we now have the SunCal matter.

25 (Pause)

1 MR. PEREZ: I meant U.S. Attorney, not U.S. Trustee.
2 I misspoke.

3 THE COURT: Fine.

4 (Pause)

5 MR. PEREZ: Your Honor, the next two matters on the
6 morning docket are the motion to settle with the SunCal
7 trustee, and then the last matter is just the motion for relief
8 from stay that has been continued, obviously to the extent,
9 depending on the Court's ruling, that motion will be moot, and
10 there was no counsel for SunCal. Mr. Smiley, who was here in
11 the courtroom last time, is actually on the phone today. So
12 there was no intent ever to go forward with that motion, but it
13 was just carried along.

14 Mr. Steinberg is going to take the lead for the
15 debtors with respect to the approval of the 9019 motion.

16 THE COURT: Okay.

17 MR. STEINBERG: Good afternoon, Your Honor. Arthur
18 Steinberg from King & Spalding, on behalf of Lehman Commercial
19 Paper Inc. in its individual capacity and as the agent for the
20 first lien lenders in the SunCal bankruptcy cases.

21 Your Honor, we're here today to -- for approval of a
22 settlement, which has been embodied in an amended term sheet
23 between the SunCal trustee and LCPI as the agent for the first
24 lien lenders and on behalf of itself. Your Honor had signed an
25 order to show cause scheduling this hearing for today. The

1 order to show cause was filed and served in accordance with the
2 service list required.

3 The motion has engendered four responsive pleadings:
4 one responsive pleading filed by Fidelity National; the second
5 by Gramercy Warehouse, which is the agent for the second lien;
6 the third is LBREP Lakeside SC Master I, LLC, which was the
7 equity owner of the SunCal entity that received a dividend in
8 connection with a 2006 financing; and the last pleading was a
9 pleading filed by the creditors' committee, in support of the
10 approval of the motion.

11 We filed a reply to the responsive pleadings on
12 September 20th, which included the declaration of Robert
13 Brusco, and we also amended the proposed order to try to deal
14 with some of the objections, and we filed two such amendments,
15 the first filed in conjunction with the reply, the second filed
16 last night when we had gotten a comment from the SunCal trustee
17 who said, based on the timing of when he will get his order
18 approving him entering into the settlement, that it'll probably
19 span beyond the two-year statute of limitations for the SunCal
20 trustee to bring avoiding-power claims, and asked to have this
21 order include a provision that allows LCPI to toll the statute
22 of limitations with respect to any action so that he wouldn't
23 be forced to deal with that issue as to how to preserve his
24 claims until the settlement is approved by both this Court and
25 the bankruptcy court.

1 Your Honor, yesterday the SunCal trustee, who had been
2 struggling trying to get a hearing date from his judge, filed
3 the motion to approve the settlement. The hearing date has
4 been scheduled for December 21. And he was also able to obtain
5 a hearing date of December 2nd for approval of the disclosure
6 statement, so that he is subject to Your Honor approving the
7 New York aspect of this settlement. He is going to try not to
8 lose too much time, prepare a disclosure statement over the
9 month of October so that the adequacy of that disclosure
10 statement can be heard by the judge on December 2nd. Hopefully
11 the judge will approve the settlement at the end of December,
12 confirmation will take place in the early parts of 2011, and we
13 will be able to move forward on the plan.

14 Your Honor, I think -- in assessing the settlement, I
15 think there are four basic tenets that, once accepted, the
16 approval of the settlement will flow directly from that. The
17 first is that there's no bona fide creditor of LCPI that has
18 objected to the settlement. Two, even the responding parties
19 do not contend that the settlement is unfair from LCPI's
20 perspective. Third, the settlement does not seek to adversely
21 modify any rights except the signatories to the term sheet. In
22 other words, this is a settlement between the SunCal trustee on
23 behalf of the SunCal estate, and LCPI on behalf of itself and
24 the first lien lenders. Fourth, that this settlement was
25 approached with the interest of the LCPI estate. That was the

1 basis upon which LCPI went forward and entered into the
2 settlement.

3 With those four tenets accepted, the two general
4 questions that arise in the context of a settlement: Is this
5 settlement in the best interest of the LCPI estate? And are
6 there any third-party rights that are being adversely modified
7 by the settlement? I think the answers flow to those questions
8 from those four basic tenets.

9 The reason why LCPI decided that this was a critical
10 juncture in this case and it was important to try to settle as
11 compared to further litigate these matters is viewed -- when
12 looked at, the pending litigations that already have been
13 involved for the almost two years that the SunCal cases have
14 been going on. Your Honor was the recipient of the motion to
15 lift the stay that was filed by the SunCal trustee, that was
16 filed earlier this year, asking for permission to sell the
17 properties which is the subject of LCPI's collateral and the
18 first lien lenders' collateral. Companion with that was the
19 motion filed in the SunCal case to retain a broker, which LCPI
20 did not feel was the appropriate broker. Companion with that
21 was a contract that he had entered into for the sale of the
22 properties for forty-one million dollars, which was embedded
23 with a breakup fee of a million dollars, which LCPI didn't
24 agree with. Embedded in that was the request to strip the
25 first lien lenders of their rights to credit-bid, which LCPI

1 wasn't in favor of. And embedded with that was an attached
2 draft equitable subordination fraudulent transfer complaint,
3 which they wanted to be able to bring for purposes of
4 determining liability. So that was one critical juncture that
5 we had to decide whether we will face the litigation head-on,
6 whether we would use this opportunity to try to settle.

7 The second thing is that in the SunCal cases there
8 have been pending disputes that have lasted over the 2010 year
9 with regard to use of cash collateral. Since the filing of the
10 SunCal cases, there's been approximately 4.8 million dollars of
11 cash collateral that is being used for purposes of preserving
12 the properties. It seemed like that, if we didn't do
13 something, that that cash collateral, which would otherwise be
14 the first lien lenders' collateral, would be dissipated further
15 and further. The case started with about a little over
16 eighteen million dollars of cash collateral and now it's been
17 reduced to somewhere between thirteen and fourteen million
18 dollars. So there was a desire to preserve the cash collateral
19 and to sell the properties or to put it into an appropriate
20 position to sell to preserve as much of the cash collateral.

21 The first lien lenders, in 2008, had filed a motion in
22 the SunCal case to lift the automatic stay. That was basically
23 taken -- put in suspense while the settlement negotiations were
24 going on. But if this case was not going to settle, that
25 motion would be resumed. That motion subsumed lifting --

1 modifying the stay on two grounds: One ground was lack of
2 adequate protection, but the second ground was that the debtor
3 had no equity in the properties, which I think has been
4 admitted, and that the properties are not necessary for an
5 effective reorganization. No doubt that the pursuit of that
6 automatic-stay litigation would lead to competing plans and
7 further litigation expense. And this case has become more
8 complicated, because it's not all concentrated before one
9 bankruptcy court; it spans two bankruptcy courts, with both
10 bankruptcy courts represented by -- with fiduciaries in both
11 bankruptcy courts trying to advocate the positions on behalf of
12 the estates that they're to represent.

13 So this was a critical juncture in this case, and we
14 are approaching the two-year anniversary for purposes of
15 bringing avoiding-power claims in the SunCal case. And if we
16 hadn't agreed to toll -- tolling is just a Band-Aid.
17 Ultimately you have to address the merits of the claims or not.

18 From the beginning of the case, or very shortly after
19 the beginning, the decision had been made by LCPI to try to get
20 a settlement. And I think Your Honor is familiar with the fact
21 that there was an extensive period of time that had been
22 engaged in to try to negotiate what our papers call the
23 original term sheet. After the trustee -- the SunCal trustee
24 had filed a motion in the California court, it had engendered
25 some objections. The SunCal trustee reviewed his -- the

1 original term sheet; was concerned as to the ramifications if
2 there were senior liens that were not otherwise covered by
3 title insurance that were greater than a million and a half
4 dollars; did not like necessarily what those ramifications are.
5 He said there was an ambiguity; case got off track; and that
6 precipitated the SunCal trustee motion, the hearing before Your
7 Honor, where Your Honor urged the parties to settle, which
8 brings us to here today.

9 From LCPI's perspective, the benefits of a settlement
10 are clear. With a settlement, there's a obviously a reduction
11 of the expenses that have been incurred on behalf of the first
12 lien lenders in the case, because you're resolving a
13 significant amount of the litigation that I've outlined before,
14 and you are exchanging general releases. You are avoiding the
15 litigation risk that's involved in any type of case that's
16 before.

17 And just as significantly, this litigation has created
18 a stalemate in the disposition of not just the cash collateral
19 account but the real-estate property itself because until some
20 of these issues are resolved the property just sits. The
21 property then subsumes a further negative connotation in the
22 market. And most importantly, if there was a realization
23 opportunity, a favorable realization opportunity for the
24 properties, you could potentially lose it as you engage in
25 further protracted litigation as both parties try to gain the

1 system, leverage each other in order to try to drive to a
2 resolution that they otherwise would have.

3 So the settlement that has been entered into basically
4 gives two bundles of rights to the LCPI estate in two different
5 time periods: one is the settlement effective date and the
6 second is in conjunction with a plan of reorganization. On the
7 settlement effective date, which is when Your Honor will have
8 approved, if Your Honor approves the settlement, and the SunCal
9 trustee bankruptcy court approves the settlement, at that time
10 the cash collateral account will effectively been allocated in
11 accordance with the term sheet where leases will have been
12 exchanged and litigation will have stopped. Those things will
13 have been put in place. The claims of LCPI in the SunCal case
14 will have been recognized and the claim that the SunCal trustee
15 filed in the LCPI case will have been withdrawn. All of those
16 things take place as of the settlement effective date. Then
17 under the plan of reorganization the properties will be sold,
18 and the trustee is contractually obligated to proffer a plan
19 which will provide for the sale of the properties for the other
20 assets of this estate to essentially be divided fifty percent
21 to the first-lien lenders, which includes LCPI, and fifty
22 percent to, in effect, the trade creditors. That contemplates
23 the enforcement of the intercreditor subordination agreement
24 between the first-lien lenders and the second and third-lien
25 lenders.

1 In this case the first-lien debt is about 235 million
2 dollars; the second-lien debt is 85 million dollars; the third-
3 lien debt is 75 million dollars. The total lien debt in this
4 case is 395 million dollars. The overall claims in this case
5 is about another 60 million or 455 million dollars. The lender
6 group is the predominant class in the SunCal case. A give-up
7 of what otherwise would be given to the first-lien lenders by
8 enforcement of the subordination to get to the fifty-fifty
9 level is a give-up.

10 The settlement also contemplates what might happen if
11 we could not enforce the intercreditor agreement, if the
12 second-lien lenders or the third-lien lenders could effectively
13 make an argument. They will have that opportunity to make that
14 argument in the context of the SunCal plan of reorganization.
15 If that happens, the settlement provides that LCPI, who is a --
16 about a twelve million dollar holder in the second-lien debt
17 and almost fifty million dollars in the third-lien debt, and
18 the first-lien lenders who hold 235 million dollars, will
19 dedicate their claims back to the trustee in order to
20 effectuate the same fifty-fifty split. Those issues will be
21 resolved as part of the SunCal plan. But either way you work
22 it, because of the mathematics and the size of the first-lien
23 debt and the LCPI positions in the second and the third-lien
24 debt we'll be able to effectuate the fifty-fifty split that's
25 contemplated by the other recoveries.

1 So Your Honor, just to highlight the benefits of the
2 settlement -- and I know I've said it before but I just want to
3 emphasize again -- it's the ability to realize the full value
4 of the properties, when we think it should be sold, with the
5 broker that we think it should be sold.

6 We've agreed to be the stalking-horse bidder, at a
7 minimum, or to say that if the SunCal trustee needs us we will
8 be the stalking-horse bidder at forty-five million dollars
9 which is four million dollars than the bid that he otherwise
10 had before. We agreed to an allocation of the monies that are
11 being used for cash collateral. That allocation is essentially
12 to give the SunCal trustee three and a half million dollars.

13 Plus agree we're no longer fighting about cash
14 collateral. You have a dedicated fund of another two million
15 dollars to take you through the set -- from the settlement
16 effective date to the disposition of the real estate. If
17 there's any money left over that flows back to the first-lien
18 lenders. The burn rate of cash collateral in this case has
19 been a little over two million dollars a year. It's
20 anticipated that we will not have another year gap for the sale
21 so there will be some money flowing back.

22 The three and a half million dollars which is being
23 given to the SunCal trustee is necessary because we're selling
24 the real estate through a plan. The reason why we're selling
25 the real estate through a plan instead of a 363 sale is that

1 the SunCal case is in the Ninth Circuit. The Clear Channel
2 decision has created some difficulties with buyers looking at
3 whether they can get something free and clear, and the decision
4 was made that in order to have the best type of result for
5 marketing the property we do it through a plan.

6 One of the byproducts of doing it through the plan is
7 that the SunCal trustee needs enough money to pay
8 administrative expenses. As a practical matter, he has not
9 really gotten very -- he hasn't really gotten paid. Creditors'
10 committee counsel really hasn't gotten paid in the two years of
11 this case. There's a loan that Gramercy made, which is the
12 second-lien agent, at the beginning of this case which would
13 have to be paid. There's plan disclosure statements, sale
14 expenses, objections to claims expenses, assisting us on the
15 resolution of the senior lien issue; all of those are
16 administrative expenses.

17 I don't think there's a lot of fat left over for
18 anything, but it was necessary to give that sum of money, and
19 that sum of money is a half a million dollars more than the
20 original term sheet. It was deemed, because he may have to
21 deal with the broker who won't have the same deal that he
22 thought he had, that he may have to deal with the contractual
23 bidder that has never been approved, that he may have to deal
24 with something like that. We gave him the money so that he
25 could administer the case and confirm a plan pursuant to which

1 the real estate, which is the primary collateral, would be
2 sold.

3 Those are our benefits. The detriments that we gave
4 up are we gave up some of our cash collateral. But we have
5 been fighting cash collateral for two years already in this
6 case. We've already had a 4.8 million dollar dissipation of
7 cash collateral. We gave up 3.5 percent of the net proceeds
8 that we would get under the real estate.

9 Now, we said we would be a stalking-horse bidder for
10 forty-five million dollars. There are potentially senior
11 mechanics' liens which would be ahead of us. To do simple
12 math, if the net purchase price would be fifty million dollars
13 because we were able to get a deal that reflected that amount
14 of money net to us, net of the brokerage fee and everything
15 else, 3.5 percent would be 1.75 million dollars to the SunCal
16 estate and 48.25 million dollars for the benefit of the first-
17 lien lenders. In the context of a compromise that was deemed
18 to be sufficient from LCPI's perspective. And I think no one
19 is challenging that LCPI is having at least a fair deal in the
20 matter.

21 There are the three responsive pleadings, other than
22 the committee that is supportive of the transaction. One was
23 filed by Fidelity, and I think that's probably the easiest to
24 deal with because Fidelity perceived an ambiguity which we,
25 frankly, didn't think existed. But for purposes of clarifying

1 the record, and we put it in our reply, that when we said that
2 the SunCal trustee was going to cooperate in trying to deal
3 with the senior lien issue that was not meant to say that the
4 first-lien lenders, who in effect purchased the title policy,
5 would not live within its contractual commitments for
6 cooperation. The bargained-for rights for the SunCal trustee
7 was additive. So it was not only that the first-lien lenders
8 will do something but if it didn't cost an extreme amount of
9 money the SunCal trustee would also cooperate to allow us to
10 resolve the mechanics' lien issues which are the creditors of
11 the SunCal estate.

12 So we clarified that. I make the statement on the
13 record. With that statement, I think, we've spoken to them
14 before, I think they're here today, everything else they said
15 in their pleading was a reservation of rights, the same type of
16 reservations of rights that they sent to the first-lien lenders
17 over a year ago, to the counsel that was handling mechanics'
18 liens issues saying that there are some potential defenses we
19 have, we'll defend you, we'll stand -- we'll continue to defend
20 you now, but we're reserving our rights because we haven't
21 crossed the bridge on that yet.

22 And they said please, Your Honor, although we're
23 saying to you, sir, as we're reserving our rights, we're not
24 asking you to rule on any of those reservations of rights in
25 connection with the settlement agreement. And generally we are

1 supportive of the settlement, it cleans up most of the
2 objections, and subject to cleaning up the ambiguity that I
3 referred to before we're generally supportive of the settlement
4 agreement.

5 So I was careful to call them responsive pleadings
6 instead of an objection because I didn't want to overstate what
7 Fidelity had. They, like a lot of title insurance companies,
8 they put their marker down saying I'm still holding on to my
9 bundle of rights, rights which we totally disagree with and we
10 think at the end of the day we will win, but there's no reason
11 to deal with that in the context of this motion because they're
12 not asking you to, I don't think we have to, and it's not an
13 impediment to the settlement.

14 THE COURT: Let me stop you for a second. You've been
15 talking for quite awhile, Mr. Steinberg. Is the Fidelity
16 objection a live objection at this point?

17 MR. COHEN: Good afternoon --

18 THE COURT: If you say no that'd be great.

19 MR. COHEN: Good afternoon, Your Honor. Joshua Cohen
20 from Day Pitney, on behalf of Fidelity.

21 With respect to the issue of the duty to cooperate,
22 Mr. Steinberg's representations on the record and the
23 statements that were made in the reply do address those issues
24 and address the objection that was asserted with respect to
25 that. So with respect to that issue, Your Honor, the answer is

1 no.

2 We do have reservations of rights that we would like
3 to address on the record, whether Your Honor wishes to do it
4 now or following the rest of the presentations --

5 THE COURT: Well, we've been going for a long time and
6 we're kind of at a point where we're either going to get this
7 done before I break for lunch, because I have a 2 o'clock
8 calendar, or we're going to carry this to the afternoon
9 calendar. And so I need to get some sense as we go, objection
10 by objection, whether or not I'm going to have what amounts to
11 lengthy argument with respect to the objections or whether or
12 not these are just going to be statements, reservation of
13 rights type objections.

14 I suspect the fact that both Mr. McKane and Mr. Basta
15 are in court today indicates either they don't have that much
16 to do right now or they're going to be pressing their
17 objections on behalf of LBREP vigorously which suggests to me
18 that I may be taking a lunch break, it's just a question of
19 when. Unless -- there's somebody standing in the gallery --

20 MR. DURRER: I apologize for rising, Your Honor. I
21 have a suggestion that I think will address Your Honor's direct
22 question about schedule.

23 THE COURT: What, about lunch?

24 MR. DURRER: No, Your Honor. It'll actually allow the
25 conclusion of these proceedings instantly.

1 THE COURT: Okay, let's hear what that might be.

2 MR. DURRER: Thank you, Your Honor, I appreciate that.
3 Van Durrer, Skadden Arps Slate Meagher & Flom on behalf of
4 Gramercy Warehouse Funding I, LLC, the second-lien agent, as
5 Mr. Steinberg mentioned.

6 Your Honor, I know that the debtors had filed on
7 Monday a declaration of Mr. Brusco. We have reviewed it. I've
8 cobbled together a cross-examination of Mr. Brusco which I'm
9 prepared to go forward with today. But my understanding under
10 Local Rules is that this would not be an evidentiary hearing.
11 Given that the SunCal matter in California is set for hearing
12 on December 21st, it doesn't seem to me that there is any rush,
13 nothing's going to happen for several months in any event, so
14 that if we could schedule an evidentiary hearing so that
15 discovery can be taken, if appropriate, and we can brief any
16 issues that Your Honor identifies or that the parties think
17 would be appropriate --

18 THE COURT: That doesn't sound like an instant
19 resolution at all. That sounds like stretching this out to the
20 detriment of the parties, and I appreciate your stepping up at
21 12:30 to make that proposal, but you can sit down.

22 MR. DURRER: Thank you, Your Honor.

23 THE COURT: We're not doing that. We're going forward
24 and we're taking a lunch break. But I want to take a lunch
25 break at an appropriate time which would be after Mr. Steinberg

1 has completed his recitation as to the current status of things
2 and parties who are represented who are objectors with live
3 objections can at least state what their intentions are or
4 whether or not they agree with what's been said. And we're
5 then going to resume at 2 o'clock immediately after the
6 2 o'clock status conference which involves one of the adversary
7 proceedings and shouldn't take terribly long. So I have time
8 this afternoon to hear you.

9 MR. STEINBERG: Thank you, Your Honor. With respect
10 to Fidelity, they did, in addition to their reservation of
11 rights, say that there were two ambiguities. And one related
12 to if we do a sale free and clear of liens except for permitted
13 liens, as contrasted to senior liens, permitted liens being the
14 kind of things like easements, et cetera, they said that that
15 word is kind of used loosely and we accept their comment and
16 when the sale motion is filed or is embedded in part of the
17 plan we will be careful of how the permitted liens are defined
18 so we don't have a circular type definition.

19 As far as their saying that they haven't committed to
20 give title insurance to any potential buyer for the property we
21 accept that notion that they haven't committed to give title
22 insurance.

23 With regard to the objection filed by Gramercy, the
24 second-lien agent, they raised three objections, two of which
25 we've resolved pursuant to the proposed order. One related to

1 the clause in the proposed order that said that there was a
2 retention of jurisdiction to this court. They were concerned
3 that that type of what I thought a plain vanilla clause could
4 potentially undermine the jurisdiction of the California court.
5 And they asked us to include language that says that nothing is
6 intended to undermine and affect the exclusive jurisdiction of
7 the California court and whatever those issues are or to
8 predetermine any concurrent jurisdiction issues. And we were
9 prepared to live with that language. Obviously, it's Your
10 Honor's order, but we would find that acceptable.

11 The second was they looked at a page in the amended
12 term sheet, they flipped seven pages later, they said 'Ah-hah,
13 I think there may be another ambiguity. Can you potentially
14 clear it up?' They suggested some language. We accepted that
15 language. The language specifically said that, in essence,
16 that nothing in this term sheet is intended to, in effect,
17 adversely modify the rights of any party who wasn't settling.
18 So we weren't trying to predetermine any rights that the first-
19 lien lenders had as against the second-lien lenders. We were
20 simply settling our disputes between the SunCal estate and the
21 SunCal trustee and LCPI. So we accepted their language and
22 they're fine with that.

23 So then the third thing is really not an objection,
24 and they really do not have standing for anything in this case.
25 They are not a creditor of LCPI. They are a creditor of the

1 SunCal estate which is a disputed creditor of the LCPI estate.
2 Their argument -- and it's not even an objection because they
3 say basically, 'Judge, we're trying to be helpful here' -- sort
4 of like the same kind of help that they had about the
5 adjournment -- 'We're trying to be helpful here. What we think
6 is that the SunCal trustee hasn't done his job. He hasn't done
7 his diligence. Man, if he did more diligence he'd be able to
8 find bigger claims against the LCPI estate. He'll never win in
9 the SunCal court, so let's assume he's not going to win and
10 let's deal with that issue automatically right now. Let's lift
11 the stay, let the SunCal trustee take more discovery on the
12 claims that he's otherwise settling or let's appoint another
13 examiner in this case. Let's have the LCPI estate bear greater
14 administrative expenses as a helpful suggestion by a
15 noncreditor of the LCPI estate, all for the purpose of
16 establishing larger claims against LCPI and undermining the
17 settlement.'

18 Well, I think that argument is probably a very good
19 argument in support of the settlement because he's essentially
20 conceded, without being a party-in-interest in this case, that
21 this is a good settlement for LCPI. And that is what we're
22 asking Your Honor to evaluate. But certainly I don't think he
23 has standing to object. Once we said that there's nothing in
24 this case that's affecting his rights then we don't think that
25 he has standing to say anything in this case at all.

1 And I think, just to put it on the table, he's being
2 helpful because he is a party, his client is a party to an
3 intercreditor agreement that says that "The second-lien agent
4 will not contest or support any person in contesting in any
5 proceeding the priority, validity or enforceability of a lien
6 held by the first-lien lender claim holders in their first-lien
7 collateral." So he's skating very close to it, and so as a
8 nonparty to this action he's coming forward with this type of
9 helpful suggestion.

10 With regard to LBREP Lakeside, they are not asserting
11 that this settlement is unfair to the creditors of LCPI. They
12 are not criticizing LCPI's decision to settle claims asserted
13 by the SunCal trustee. In reality, their only complaint is
14 that they're not getting a settlement as well too; they want a
15 settlement. It would be nice if they settled but there is no
16 settlement on the table right now. They value their claim at
17 zero. The SunCal trustee values their claim as something more
18 than zero. They haven't been able to bridge the gap.

19 But there's nothing in this settlement that prevents
20 LBREP from settling with the SunCal trustee. There's nothing
21 at all that affects their rights. They could do it tomorrow.
22 They could do it next week. They could do it before December.
23 We can't force the SunCal trustee to settle with LBREP.
24 Certainly we can't force it to settle it at a zero number. And
25 there's nothing in the amended term sheet that is preventing

1 them from settling.

2 They've conjured up a whole bunch of arguments, none
3 of which are grounded in any type of law. Since we say that
4 there's nothing in this settlement that's affecting any of
5 LBREP's rights they still somehow say that based on some law
6 which isn't apposite that we are profiting from our wrongdoing
7 because we're settling on the loans that we made while they're
8 still exposed on the dividend recap. The cases that they cite
9 all relate to one party directly suing another party.

10 THE COURT: I read the footnote that included some of
11 the very interesting cases that were cited --

12 MR. STEINBERG: Okay, so --

13 THE COURT: -- involving photographs and real contests
14 and the like.

15 MR. STEINBERG: So the general obligation law citation
16 which is really just a bootstrap of the same argument that you
17 shouldn't be able to profit from the other: (a) we don't have
18 a litigation; (b) we're not asserting contribution claims; and
19 (c) even if we had -- if we were joint tortfeasors and we were
20 asserting contribution claims they get the benefit of the
21 reduction of their liability under New York general obligations
22 law.

23 THE COURT: Okay.

24 MR. STEINBERG: You heard that part. All right, so
25 then I'll leave with the last two arguments that they have.

1 THE COURT: I actually read the papers.

2 MR. STEINBERG: Okay. So then I'll just -- Your
3 Honor, just the last two things, and maybe I'll just flag them
4 and if Your Honor has any questions, because I think our papers
5 adequately dealt with them. One was if we settle, after having
6 staked out all of our position in the SunCal estate, if we
7 settle and say that we never believed that this litigation had
8 any merit but we suddenly change our position because we are a
9 potential recipient of the other recoveries, will we perjure
10 ourselves, violate the federal rules based on this concern.
11 And I think that is clearly a nonmeritorious objection, and our
12 papers recite why we would uphold the oath, the ability to tell
13 the truth, et cetera, et cetera.

14 And the last thing that they say is that there's a
15 conflict of interest. And really the biggest example of why
16 there's no conflict of interest is they're in court today.
17 Right? They're objecting to the settlement. We're not
18 controlling them. We didn't undermine any aspect of their
19 settlement. We didn't try to affect their ability to settle at
20 all. They are -- you know, the LBREP or the Lehman estate
21 entity is a minority economic interest in LBREP. It's -- the
22 majority or the clear majority is held by third parties. In
23 the LCPI, for the first-lien lenders the LCPI estate is only
24 thirty percent of the first-lien lender debt. There are all
25 these outside third parties that are making sure that their

1 individual parochial rights are being protected. There is
2 nothing in here as a bottom line that's prejudice. And we said
3 it at the beginning and the basic tenet is that we approach
4 this settlement from the perspective of LCPI. We didn't
5 approach it from the perspective of LBREP. We did it on behalf
6 of LCPI who is the individual lender and is acting as an agent
7 for the first-lien lenders.

8 Your Honor, our papers do recite the general standards
9 that I know you're familiar with about lowest range of
10 reasonableness, canvassing of the issues, et cetera, and we
11 think we've clearly met that burden in this case.

12 THE COURT: Okay, thank you.

13 I want to hear, before I hear from LBREP Lakeside,
14 from Mr. Smiley if he's on the line.

15 Mr. Smiley, are you there?

16 MR. SMILEY: Yes, I am, Your Honor. Good afternoon.
17 Your Honor, I don't have much to add on behalf of the SunCal
18 Chapter 11 Trustee. I just would point out that this
19 settlement is supported by both the Chapter 11 Trustee of the
20 SunCal estates, by the creditors' committee in our estates,
21 obviously by the debtor in your estates and the creditors'
22 committee in your estates. And --

23 THE COURT: That's helpful. Let me ask you one
24 question because counsel for Gramercy made another one of his
25 helpful suggestions in proposing that maybe we could just end

1 this whole thing, go to lunch, and do this another day. And I
2 told him that I thought that wasn't a good idea and I proposed
3 that he take his seat again. I see him smiling, at least, in
4 the courtroom right now.

5 One of the reasons that I made that judgment -- I want
6 to verify this with you -- is that my conclusion from what Mr.
7 Steinberg said about the scheduling of this in California is
8 that things need to move forward on the assumption that you
9 have a settlement that's at least approved here, and that in
10 order for you to be undertaking the work necessary for plan
11 disclosure statement purposes you really need to have that
12 certainty, and that delay here would lead to delay in
13 California. I want to confirm that that assumption on my part
14 is correct.

15 MR. SMILEY: Your Honor, your assumption is correct.
16 Although we have a December 21 date before Judge Smith and we
17 did try to get an earlier date, we went ahead and filed our
18 compromise motion almost ninety days early so that if there's
19 discovery, if there's issues that need to be addressed that
20 they can be addressed in our estate. And in addition to that,
21 given that there is a drop dead date of February 28th to
22 confirm a plan, we do need to proceed right away with filing
23 the plan of reorganization, and we anticipate having that filed
24 by probably mid to late October. So timing is an issue.

25 Another important note is we have a potential

1 stalking-horse bidder that was proffered in connection with our
2 original motion. They are still there. There are other
3 bidders and they are all -- they all call almost every day.
4 And we need to give them answers about whether we're going down
5 this process or not. A lot of them have put a lot of time and
6 effort into reviewing these trial briefs.

7 THE COURT: Okay.

8 MR. SMILEY: So it is important that we move
9 expeditiously and that we have certainty on both coasts in both
10 cases.

11 THE COURT: All right, thank you for that. Is there
12 anything more you wish to add?

13 MR. SMILEY: No, Your Honor.

14 THE COURT: Okay. Now before we take a lunch break,
15 unless it's possible to resolve this in the next ten minutes, I
16 want to just find out from counsel for LBREP Lakeside -- is
17 there some easy way to say that? How about just Lakeside?

18 MR. BASTA: Or just LBREP -- or Lakeside's fine. Your
19 Honor, I have about fifteen or twenty minutes of argument.
20 There's no evidence. If they don't go beyond the scope of the
21 declaration there won't be any evidence; fifteen to twenty
22 minutes of argument.

23 THE COURT: Okay. And let me find out from Gramercy
24 what Gramercy really wants to do at this point.

25 MR. DURRER: Your Honor, Van Durrer for Gramercy.

1 Well, as I mentioned, Your Honor, we are prepared to go
2 forward. We will have argument. We will have cross-
3 examination of the witness.

4 THE COURT: You're perfectly permitted, in my view,
5 given the circumstances, to call the declarant. I assume the
6 declarant is in court?

7 UNIDENTIFIED SPEAKER: Yes, he is.

8 THE COURT: So his declaration, which I have read,
9 would be his direct testimony and you can ask questions on
10 cross-examination. That suggests that we should take a lunch
11 break and I'll see you back at 2 o'clock. We're adjourned till
12 then.

13 (Recess from 12:42 p.m. until 2:24 p.m.)

14 THE COURT: Be seated, please. We'll start with the
15 pre-trial. Do we have counsel for Michigan State Housing?

16 UNIDENTIFIED SPEAKER: Your Honor, they're just
17 conferring in the hallway so my colleague just went to ask them
18 to come in.

19 THE COURT: Okay.

20 (Pause)

21 MR. ALBANESE: Good afternoon, Your Honor.

22 THE COURT: Good afternoon.

23 MR. ALBANESE: Anthony Albanese on behalf of the
24 debtors in connection with the Michigan State matter.

25 We're here for a conference with the Court. Your

1 Honor, the matter -- this adversary proceeding has been stayed
2 a number of times pending the parties' attempt to mediate the
3 dispute. Most recently the stay was in fact up until July
4 15th. Our adversary, Michigan State, who I'll turn it over to
5 in a moment, had not agreed to extend the stay at that point in
6 time because they wanted to see more movement on the mediation
7 front. The parties had conferred several times in an
8 attempt -- without a formal mediator in an attempt to move the
9 ball forward.

10 THE COURT: This is a mediation without a mediator?

11 MR. ALBANESE: Correct. We were --

12 THE COURT: That's not mediation.

13 MR. ALBANESE: Well, we now have a mediator. My next
14 point, Your Honor, is that we now have a mediator. They've
15 been appointed. We've been waiting for one to be appointed but
16 we're trying to move the ball forward in the interim. A
17 mediator has now been appointed; we just learned yesterday who
18 the mediator would be. And the mediator has proposed three
19 dates in the end of October and the beginning of November. The
20 debtor is available on all three dates. Michigan is
21 determining which of those dates they're available on.

22 So the debtors request that the matter, the adversary
23 proceeding, be stayed at least pending the mediation which
24 should occur within thirty days. And Michigan State has not
25 yet agreed to consent to that stay, but I'll turn the floor

1 over to them. But at this point it does not seem to make sense
2 for the debtors to spend any time and money engaging in
3 discovery the next thirty days in the adversary proceeding not
4 that we do in fact have a mediator and have three proposed
5 dates which the debtors have agreed to all three dates.

6 THE COURT: Okay. Where's Michigan State? Please
7 identify yourself for the record.

8 MR. MURPHY: Good afternoon, Your Honor. Michael
9 Murphy appearing on behalf of the Michigan State Housing
10 Development Authority.

11 We just got -- I think it was just last night that
12 some e-mail came through with so-called dates for the
13 mediation. One of our concerns has been, consistently all
14 through this process, is that to mediate this meaningfully to
15 hopefully get a resolution out of mediation we need certain
16 information to be able to have an effective mediation. We've
17 never been able to get that. We've had a couple of informal
18 conferences over the phone. We've had various agreements that
19 have fallen apart over this period of time about exchanging
20 certain information. We did submit significant information to
21 Lehman Brothers based upon how we calculated our termination
22 payments. They said they would simultaneously give us their
23 information. We got two pages from them of just nothing that
24 we could work with or figure out.

25 So we had another phone conference subsequent to that.

1 We did make some headway narrowing the issues. But the problem
2 is, is I know the Court wants to, and we've agreed to, and I
3 think it's a very good idea to try to mediate the dispute. But
4 if you can't get information to be able to effectively mediate
5 it then we're wasting everyone's time. So we were trying to
6 get some discovery to get this information and we've conducted
7 most of the criteria in Rule 26 which allows -- you know, we've
8 done certain things as far as exchanging and swapping
9 information. We've prepared a discovery plan. We have
10 submitted it to them. We're waiting for comments. To stay the
11 matter thirty days and then go to mediation without information
12 that we think we need to effectively mediate it means we're
13 going to spend a whole day at the mediation and not be able to
14 accomplish much. So that's why we haven't agreed to the stay.

15 THE COURT: Well, whether you agree to it or not,
16 there isn't going to be a lot of activity in the litigation
17 unrelated to preparing for the mediation if you're both
18 agreeing to mediate. So I think it's largely an academic
19 issue.

20 Also, I looked at the pleadings here, and if I
21 understand correctly what's going on, you're seeking to recover
22 a 2.4 million dollar, more or less, payment that was made to
23 Lehman allegedly by your trustee that shouldn't have been made.
24 But your trustee isn't a defendant. Why is that?

25 MR. MURPHY: There's been some discussion with our

1 clients as regarding their relationship with the trustee and
2 the bonding thing and they don't feel that the trustee should
3 be brought in at this time as a defendant, and so I've honored
4 their wishes.

5 THE COURT: I consider that curious, to say the least.
6 If the payment was allegedly made improperly by the trustee you
7 may not have all the parties before the Court or before the
8 mediation who may have potential financial responsibility.

9 Also, I see that there is a counter-claim, although
10 it's unclear to me from the counter-claim what the damages
11 might be based upon your calculation of termination payments.
12 And I would hope that at least the parties would exchange that
13 much information so you know what your exposure is in this case
14 just in case you might be on the wrong end of it.

15 Do you know what your exposure is in this case?

16 MR. MURPHY: Yes, we do, based upon the ADR submittals
17 that Lehman Brothers have already made.

18 THE COURT: Then you probably know what you need to
19 know.

20 MR. MURPHY: Yes, at least we have a pretty good idea.

21 THE COURT: Okay. What do the parties want from me at
22 this conference?

23 MR. ALBANESE: Your Honor, I would suggest that we set
24 a conference for after the mediation which will occur about
25 November 5th. And hopefully we'll resolve it, we'll continue

1 our discussions before and during the mediation, and if not
2 then we'll come before Your Honor with a discovery schedule.

3 THE COURT: Fine, that makes sense.

4 MR. ALBANESE: Thank you, Your Honor.

5 THE COURT: And to the extent that there is a need for
6 some informal information in order to make the mediation
7 productive, I assume that the parties will cooperate with one
8 another in providing the information necessary to make the
9 mediation a productive experience for all parties.

10 MR. ALBANESE: We will, Your Honor. And our last
11 call, I think we agreed was our most productive, so we'll
12 continue in that -- down that path.

13 THE COURT: Good. You're moving in the right
14 direction. Okay.

15 MR. ALBANESE: Thank you, Your Honor.

16 MR. MURPHY: Thank you.

17 THE COURT: Now we'll pick up with LBREP.

18 (Pause)

19 THE COURT: Was any progress made during the lunch
20 break?

21 MR. STEINBERG: Your Honor, I think at this point in
22 time you had indicated you wanted to hear from the objectors.
23 With regard to the second-lien agent, Gramercy, we had
24 indicated that we had questioned whether they had any standing
25 to -- at this point in time. Even if Your Honor was prepared

1 to hear them out for the completeness of a record, I'm not sure
2 what is left of their objection because if Your Honor -- and I
3 think at the morning hearing didn't accept their helpful
4 suggestions then I think we resolved those aspects that they
5 objected to and I don't think they have anything left in their
6 objection that they've filed that they're objecting to the
7 settlement, and they are the only person asking to examine a
8 witness. So before we hear from the objectors it would be
9 helpful to figure out what is it that the second-lien agent is
10 objecting to at this point in time.

11 THE COURT: Okay. I'm prepared to hear from them what
12 it is that they're objecting to --

13 MR. STEINBERG: Thank you.

14 THE COURT: -- at this time and also to hear on what
15 basis they claim to have standing to object in the first
16 instance.

17 MR. STEINBERG: Thank you, Judge.

18 MR. DURRER: Good afternoon, Your Honor. Van Durrer,
19 Skadden Arps Slate Meagher & Flom, on behalf of Gramercy
20 Warehouse Funding I, LLC.

21 With regard to our standing, Your Honor, I think that
22 the answer is pretty simple. Mr. Steinberg has already
23 mentioned, and it's not disputed, that Gramercy as second-lien
24 agent and LCPI as first-lien agent, among others, are parties
25 to an intercreditor agreement that was entered into early in

1 2007 that governs the rights and obligations and duties among
2 the parties.

3 THE COURT: Do you have any claims in the LCPI case?

4 MR. DURRER: We do, Your Honor.

5 THE COURT: What are they?

6 MR. DURRER: The claims would be for breach of that
7 agreement and/or for breach of the duty of good faith and fair
8 dealing that arises under that agreement under New York law and
9 also California law by entering into the settlement.

10 THE COURT: Did you file a protective proof of claim
11 to cover those claims?

12 MR. DURRER: We did not file a protective proof of
13 claim, Your Honor, because under the Ninth Circuit law those
14 actions, because they arise -- well, first of all, we didn't
15 file one under the intercreditor agreement because this issue
16 hadn't arisen. With regard to the underlying actions, which
17 is --

18 THE COURT: Do you claim that this settlement
19 agreement violates the intercreditor agreement?

20 MR. DURRER: I may, Your Honor.

21 THE COURT: Well, but -- well, you may; do you?

22 MR. DURRER: I've not yet had an opportunity to
23 examine the witness or depose the witness. I just got the
24 declaration for the first time a couple of days ago and there
25 are issues that arise in that declaration that give me pause

1 regarding the good faith nature of this negotiation and the
2 entering into the settlement by LCPI.

3 The other claims that we have, independent from the
4 intercreditor agreement, are the same claims that are being
5 released by the settlement. The reason why we didn't file a
6 proof of claim with respect to those, Your Honor, is that under
7 Ninth Circuit law when the order for relief was entered and the
8 trustee was appointed we were divested of those claims, they
9 were taken over by the SunCal trustee, and it would have been a
10 stay violation for me -- in that case for me to file a proof of
11 claim in this case and assert dominion and control over those
12 causes of action.

13 THE COURT: It sounds to me that you don't have any
14 claims. You've just said that those claims were divested and
15 became claims of the trustee under Ninth Circuit law, so
16 haven't you just said you don't have standing?

17 MR. DURRER: No, Your Honor, because we still have --
18 first of all, standing is broader than having a claim, in the
19 first instance. Standing as a creditor is also broader than
20 having filed a proof of claim. The settlement, I believe,
21 based upon what I've heard so far, and I want to test it by
22 asking the witness some questions, I believe may negatively
23 impact our rights under the intercreditor agreement.

24 And I mean, there's no doubt that we are a party to an
25 agreement with this debtor. I think that under 1109, if not as

1 a claim today, that clearly gives us standing to ask questions
2 about a settlement that hinges upon the operation of the
3 intercreditor agreement itself.

4 And the fifty-fifty split, Your Honor, that is a
5 component of the settlement, it requires that LCPI and the
6 SunCal trustee win an argument against me that I'm not entitled
7 to proceeds of certain recoveries by virtue of that agreement.
8 And I believe that entering into that agreement without even
9 consulting with us at all as a party-in-interest potentially
10 violated their duty of good faith and fair dealing. I think
11 that that --

12 THE COURT: Which bankruptcy court would be the right
13 court to decide whether or not you have a claim?

14 MR. DURRER: Apparently, Your Honor, I think it's a
15 question of concurrent jurisdiction. I think that either court
16 may have jurisdiction to hear that. Honestly I haven't
17 explored it in depth and research. But this is the problem
18 that we're here for, as a matter of fact, if I can address that
19 for a moment.

20 Mr. Steinberg actually used a very appropriate
21 metaphor earlier; he called this a stalemate, and it is. The
22 problem is Judge Smith in California has not let LCPI exercise
23 its remedies against its collateral because of the allegations
24 that have been made in the California court. However, this
25 Court has not permitted anyone to take discovery -- and I'm not

1 saying that Your Honor personally took an interest or invoked
2 some sort of control, but rather the debtor has invoked the
3 automatic-stay protection of this Court to prevent any party-
4 in-interest from taking any discovery, not even in their motion
5 for stay relief. They go into California court and they say
6 'I'd like stay relief. I would like relief from this court,
7 yet you cannot ask me any questions, you cannot depose my
8 people, you cannot see my documents.' That creates the
9 stalemate.

10 So we -- and I must admit that when Mr. Steinberg
11 describes my suggestions they don't sound as helpful as I
12 thought they were, but out of my own mouth, I mean, we thought
13 that let's raise our hand now and say to Your Honor, you know,
14 we have a couple of suggestions as to how to break that
15 stalemate and let this thing move forward. One suggestion was
16 lifting the automatic stay just for discovery, just for
17 discovery purposes. And we can certainly work with the other
18 side to delineate how that process goes. Perhaps we can engage
19 in it informally. So far we've been completely rebut --

20 THE COURT: What's your objection to the settlement
21 agreement, apart from these suggestions of what you want to do
22 or what relief you're seeking unrelated to the settlement
23 agreement? What is Gramercy's objection to the settlement
24 agreement that hasn't already been covered by adjustments made
25 in the order?

1 MR. DURRER: The objection we have to the settlement
2 at this point, Your Honor, based on the declaration filed a
3 couple of days ago, is that the settlement is not fair, even to
4 this estate, because it may expose the estate to substantial
5 administrative liabilities, and that it is not --

6 THE COURT: When you say "this estate", you're talking
7 about the estate of LCPI?

8 MR. DURRER: Correct, Your Honor. And that is --

9 THE COURT: So you're here as a friend of the LCPI
10 creditors?

11 MR. DURRER: No, I would rather not have to pursue
12 litigation to recover a forty million dollar administrative
13 claim in this estate. I'd rather not be here, Your Honor,
14 candidly, but for the fact that it's very close to California
15 weather here today, I would rather not, you know, dart in your
16 doorway. But our objection to the settlement is that, and that
17 the settlement has not been entered into in good faith.

18 THE COURT: All right. I'll hear what you have to
19 say, why it's time for you to examine the witness, if you
20 choose to do that.

21 MR. DURRER: Thank you, Your Honor.

22 THE COURT: Now, is there any question as to your
23 standing, Mr. Basta?

24 MR. BASTA: Your Honor, there is none. We filed proof
25 of claim 28846 in the LCPI case as a --

1 THE COURT: Well, welcome to our court.

2 MR. BASTA: Okay, thank you. It's been a year since
3 I've been here and I'm glad to be back.

4 THE COURT: Has it been that long? It hardly seems
5 that long.

6 MR. BASTA: Yes. We filed a proof of claim and that's
7 going to be the heart of my argument today because the proof of
8 claim is a protective proof of claim for contribution from LCPI
9 if it turns out that our client, LBREP Lakeside, is liable on a
10 fraudulent conveyance action. We filed a protective proof of
11 claim to make sure that the comparable recoveries are smoothed
12 out.

13 Let me just start out, Your Honor -- we have a lot of
14 respect for the folks on the other side. In fact, we work with
15 them all the time. And the reason we work with them all the
16 time is that we are a partnership. And our general partner is
17 controlled by the Lehman estate. And the Lehman estate is our
18 largest constituent. And when the dividend came out, it's the
19 Lehman entities that got the largest share of that dividend.
20 And when we want to make a major decision, we call up to one of
21 Alfredo's partners, we say, hey, look, we've got to make this
22 major decision. And he says, okay, we'll go, we'll speak to
23 the people in the Lehman estate. And the Lehman estate sort of
24 says, you can do this and you can do that. And we work it out.
25 So everything goes pretty smoothly. Sometimes.

1 Here, we've been trying to get in the door on the
2 settlement discussions. We're not naïve. I'm not here saying
3 that LCPI has a duty to bring me in to the settlement. They
4 can settle whatever they want. I've been on the other side.
5 I've been in multi-debtor cases. I'm not saying that the
6 interest of LCPI and the interest of LBREP cannot be adverse to
7 one another. That's not the position I'm taking. And it's not
8 the position that I'm taking that this is a bad settlement for
9 LCPI. I haven't looked at it from that perspective. I've
10 looked at it under Drexel and a RICO which is, does the
11 settlement adversely affect our client which is LBREP. That's
12 the focus of our objection. And our position is that based on
13 the structure of the settlement, our contribution claims
14 against LPCI (sic) are being eliminated under state law while
15 they are preserving under their settlement through the
16 structure their contribution claims against us.

17 And let me walk the Court through why this problem
18 exists. And before I do that, you know what the settlement is,
19 Your Honor. Mr. Steinberg laid it out. There's a fifty-fifty
20 split on -- they get fifty percent of the proceeds from the
21 litigation against my client, LBREP Lakeside, on the dividend
22 recap. They get fifty percent direct interest. So if the
23 trustee wins in the fraudulent conveyance claim against us,
24 LCPI and the other lenders, these -- LCPI structured the deal,
25 sized the debt, syndicated the loan, sold the loan with the

1 purpose of it being a dividend. They get fifty percent of the
2 recovery against us.

3 The term sheet says they get a fifty percent recovery
4 in other recoveries. It's misleading, Your Honor. There's two
5 assets of this estate. There's the real estate which is being
6 sold and they've reduced their secured claim to forty-five
7 million dollars so that they can get somebody to come in and
8 bid. And there's a lawsuit against us. And it's not in -- of
9 the recovery because it's not a different lawsuit. It's not a
10 different set of facts. There's one set of facts. There's a
11 dividend recap. They sued LCPI and they sued the lenders. And
12 they've threatened to sue us and they haven't done it yet but
13 they've shown us the draft of the complaint. It's the same
14 allegations. It's the cause of action. It's just -- there's
15 nothing different about it. They're just getting released.
16 They're taking a fifty percent interest in the lawsuit against
17 us.

18 Now, I know Your Honor made the comment about those
19 cases that we cited. But what I would like to do --

20 THE COURT: I was particularly interested in the case
21 involving the photographs.

22 MR. BASTA: Oh okay. Your Honor, what I would like to
23 do, because this is basically, I think, one statute is sort of
24 the sum of my argument -- a few additional tweaks.

25 THE COURT: I don't mind hearing about the case, in

1 particular, but it just caught my eye.

2 MR. BASTA: Okay. And I'm not going to talk about
3 that case.

4 THE COURT: Good.

5 MR. BASTA: If I could hand up a copy of New York law
6 for a second?

7 THE COURT: Sure.

8 (Pause)

9 MR. BASTA: So this is a New York statute on joint
10 tortfeasor, what happens if somebody gets released. And I
11 don't think anyone can argue that Lehman isn't subject to
12 applicable nonbankruptcy law. Now what this says is what is
13 the effect of a release of a tort type claim against LCPI. And
14 so the first question is, is this really a tort. Are we under
15 this statute -- am I looking in the right place. And we've
16 cited cases, both Morgenthau and a California case, Ryan, for
17 the proposition that a fraudulent conveyance action is a tort
18 claim.

19 And there's three sections. So Section A says that if
20 they settle with the SunCal trustee, our liability is reduced
21 by the amount of their settlement. And Mr. Steinberg
22 referenced that in his opening remarks. And I'm sure the
23 SunCal trustee and LBREP at the appropriate time are going to
24 have a rigmarole about how much our liability is reduced by the
25 fact that a joint defendant settled.

1 Now look at Section B. This is absolutely critical.
2 If Your Honor approves this settlement, our proof of claim for
3 contribution against LCPI is barred by B because a settlement I
4 am prohibited from seeking contribution against LCPI if the
5 settlement is approved. Done. My proof of claim is gone. And
6 then there is what is known as the quid pro quo.

7 THE COURT: Your proof of claim isn't gone. It's just
8 that there's an affirmative defense to that claim that
9 presented --

10 MR. BASTA: There's affirmative -- well, yes. Your
11 Honor --

12 THE COURT: -- that presented a result in an objection
13 to the claim which is contingent anyway.

14 MR. BASTA: Yes. But, Your Honor, the key there is
15 that in order for them --

16 THE COURT: Because we disallowed his contingent in
17 any event.

18 MR. BASTA: Your Honor -- well, it depends what the
19 facts are at the time -- just because it's contingent it would
20 have to --

21 THE COURT: I'm not challenging the argument that
22 you're making.

23 MR. BASTA: Yes.

24 THE COURT: It's just that you -- I think you may have
25 stated --

1 MR. BASTA: I short-circuited --

2 THE COURT: -- a little more strongly than was
3 necessary.

4 MR. BASTA: That's a fair statement. I apologize for
5 doing that. It's not that --

6 THE COURT: It doesn't -- your claim doesn't just
7 disappear.

8 MR. BASTA: It doesn't disappear. But, Your Honor,
9 it's subject to them coming in -- when we can addressed in the
10 proof of claim process, it's subject to them coming in and
11 relying on 15-108(b) and saying that no matter what happens,
12 we're not entitled to prosecute that claim against the estate.

13 And the quid pro quo for this section is subsection
14 (c) because if I'm prohibited from seeking contribution against
15 them, they're prohibited from seeking contribution against us.
16 And that is the heart of it which is that what they are
17 doing -- this is one lawsuit, one cause of action -- maybe
18 multiple causes of action but the same set of facts. They are
19 entering into a settlement. They are borrowing LBREP's
20 rights -- they could borrow LBREP's rights to pursue them for
21 contribution if they're taking the fifty percent interest in
22 the lawsuit against us. And this rule is not unique to New
23 York. This is the rule in twenty-five states and in
24 California, this is also the rule. It's -- I can get Your
25 Honor the citation but it's the same rule in California.

1 THE COURT: Well, let me ask you this.

2 MR. BASTA: Yeah.

3 THE COURT: I don't want to get into what the rule is
4 in California. But is it your position that New York general
5 obligations law applies to a litigation which has not yet been
6 commenced in California with respect to real property to be
7 developed in California and loans that were entered into in
8 connection with that real property in California?

9 MR. BASTA: Your Honor, there is a choice of law
10 question. I think that our proof of claim which it has an
11 effect on is obviously subject to New York law. I think you
12 could apply California law, candidly, because -- you could
13 apply California because the property is located in California.
14 But the citation if I could get -- I'll get the citation, Your
15 Honor. I can present to the Court that the rule barring
16 contribution, our contribution claim against the estate once
17 they have settled, that rule is identical in both New York and
18 in California.

19 And, Your Honor, the -- to answer your question,
20 there's a case, and it's cited in our papers, that says that
21 the prohibition on contribution -- these rules come into effect
22 even with respect to lawsuits that have not yet been filed.
23 Meaning that, once they settle, that's a prohibition on
24 contribution. There's no requirement that a lawsuit be filed
25 in order to trigger that. And the definition of

1 contribution -- we cited these state law cases. And one of the
2 reasons we cited these state law cases is that the definition
3 of contribution is very broad because what I think the statute
4 is trying to do is they want settlements, they want LCPI and
5 SunCal to settle so we don't have to hear about this anymore.
6 But -- so you should foster that. But it's not really --
7 unless you get to the quid pro quo in (b) and (c), it's not
8 really getting rid of the litigation, because what it's going
9 to shift is that instead of them being sued by the SunCal
10 trustee, if there's ultimately a judgment, they're going to end
11 up being sued by us on behalf of figuring out who is more
12 responsible for the underlying claim.

13 There is an easier way to settle the lawsuit. The way
14 to settle the lawsuit is they compromise their claims with the
15 SunCal trustee and not create an economic interest in the
16 lawsuit against us. And this rule -- you know, we cited a lot
17 of Justice Cardozo, don't profit from your own wrongdoing. The
18 rule is, I think, a basically common sense rule. You can't
19 take advantage of the statute to get a settlement and prohibit
20 us from going against them. You can't take that benefit.

21 Okay?

22 THE COURT: Well, they cite a whole bunch of cases,
23 too, and say that this has nothing to do with profiting from
24 wrongdoing which is how we get into the photographs and the
25 Will (ph.) case --

1 MR. BASTA: Right.

2 THE COURT: -- which were cited in that footnote.

3 And -- I mean, it seems to me -- and I don't mean to make this
4 overly simplistic -- that what you really want is not so much
5 to defeat the settlement as to be benefited by the settlement.
6 You want -- the affidavit or declaration that was filed by one
7 of your colleagues makes clear in paragraph after paragraph
8 attempts to knock on the door and get into the settlement
9 discussion.

10 MR. BASTA: Let me explain why that's relevant or not
11 relevant. Mr. Steinberg discussed sort of, like, oh, we can't
12 settle. There's a bid in the ask. There's never been a bid in
13 the ask. But let me -- this is the conflict point. It's not
14 really -- I'm not really alleging a conflict of interest. I'm
15 not. This is what I'm saying. If you -- we have a bunch of
16 limited partner investors. And let's look at how they view the
17 world. They view the world -- is that LBREP isn't really
18 different than LCPI. We're both subsidiaries of Lehman
19 Brothers. Lehman Brothers is our general partner. Lehman
20 Brothers controls LCPI. And they both owe duties to their
21 constituencies for which they are the controlling party. And
22 on the LCPI side, they're being very vigilant in protecting
23 themselves. They're protecting their economic interest.
24 They're worried about their stakeholders. They enforce the
25 automatic stay when the SunCal trustee came to this Court and

1 said no, no. The automatic stay applies. You can't come in
2 and you can't affect this entity that we're in control of. But
3 they call us up and they say, wait a minute. They owe those
4 same duties to us. How come -- where is it that they're
5 fighting and saying Lehman has an economic interest in this
6 fund. Lehman has an economic interest in making sure that this
7 lawsuit doesn't deprive the creditors of the Lehman estate with
8 a recovery from this. So we are here. We are the -- we feel
9 like the neglected sibling. We are the sibling that has not
10 been protected by the Lehman estate.

11 So it's not a conflict. LCPI can do what it wants.
12 They have done a good job. They can settle with their
13 creditors. But what they're doing is something worse than
14 settling with their creditors. They're facilitating a lawsuit,
15 really, that's not meritorious against us and we are under the
16 same common control.

17 We -- they say something very interesting. And I
18 talked to Mr. Perez about this. They say they don't think
19 SunCal was insolvent at the time of the dividend. Great. That
20 was a great statement. We don't think it was insolvent either,
21 the fact that they raised the debt. But it's a single issue,
22 solvency. So why are they taking a fifty percent interest in a
23 lawsuit against an entity that they control that they don't
24 think has any merit because SunCal was solvent at the time?
25 There's only two reasons why that they could be pursuing that.

1 They're either working with the trustee to try to shake us down
2 for some recovery even though meritoriously they don't think --
3 because they've said that the company is solvent. They don't
4 think it has any merit. But they want to take a fifty percent
5 cause of action in a lawsuit that they don't think has any
6 merit. We don't think that lives up to 9019. Or, second, and
7 this is really what we think happened, this idea was the SunCal
8 trustee's idea because he said if I can get the lenders in LCPI
9 who orchestrated the transactions on the sideline with an
10 economic interest in the lawsuit, that's going to make my
11 lawsuit against LBREP Lakeside easier. And that's also not a
12 good reason to settle.

13 So our position is that the settlement agreement is
14 structurally flawed. The provision -- they should go forward
15 with the settlement. God bless them. They should cut out the
16 financial incentive that both prohibits all ability to seek
17 contribution and that results in all of the key evidence being
18 presented by people who have an economic incentive for there to
19 be a finding of a fraudulent conveyance.

20 Your Honor, there's two other points I'd like to make
21 as I forgot --

22 THE COURT: Mr. Steinberg was ready to pounce.

23 MR. BASTA: Just two other points. At the end of
24 the -- Your Honor, the provision of the California code is
25 California Civil Procedure Code 877.6. It has the same

1 provision.

2 Mr. Perez --

3 THE COURT: It's just a joint tortfeasor's release
4 provision.

5 MR. BASTA: Yeah. Mr. Perez' papers at the end make a
6 point about how they offered to us taking the LCPI recovery and
7 putting it into an escrow to accommodate what our concern is.
8 And the papers sort of suggest that we rejected it. We didn't
9 reject it. We don't understand it because, one, what about --
10 we're not just focusing on LCPI. We think all the lenders were
11 participants in this transaction. So just putting into the
12 escrow the LCPI piece doesn't really help us. We don't know
13 what standard is being suggested for the release of the funds
14 from the escrow. So we don't know how that would work. And it
15 seemed to us that what Mr. Perez was suggesting is almost like
16 we're getting a financial interest in a lawsuit against us
17 which we just couldn't figure out. So it's not that we're not
18 open to suggestions on how to structurally address the
19 settlement. We just don't know how that one works in
20 particular.

21 We also don't think Moore v. Bay is relevant to
22 anything. It's been codified as 544. Moore v. Bay just says
23 it's the trustee who brings the lawsuit. It doesn't say that
24 when the -- a particular creditor who is a joint tortfeasor
25 takes a direct financial pass-through from the trustee that it

1 gets you out of this joint tortfeasor statute. And there
2 hasn't been any presentation by the debtor as to how any of
3 this works. They don't say -- they don't make a case that this
4 statute is preempted. They don't make a case that the statute
5 doesn't apply. They don't make any case as to what's the
6 impact of our proof of claim. I mean, even if Your Honor's
7 inclined to rule against us, which we hope Your Honor won't, I
8 mean, this is -- what are our rights going forward. Is our
9 ability to go after them for contribution, is that still going
10 to be preserved? We think this whole area and how this whole
11 thing works really needs some clarification to go forward.
12 Thank you, Your Honor.

13 THE COURT: Okay.

14 MR. STEINBERG: Your Honor, I do have a lot of
15 familiarity with 15-108, having litigated the issue. So I
16 think the first element of clarity --

17 THE COURT: What issue did you litigate?

18 MR. STEINBERG: The New York General Obligations Law
19 in other matters. So I'm very familiar with this section. And
20 I know that Mr. Basta just now didn't properly cite the
21 section. And you have to go back to understand that the
22 purpose of 15-108 is to promote settlements. And it does say
23 that if one of joint tort -- one of a number of joint
24 tortfeasors that that joint tortfeasor's contribution claims
25 has against others are dismissed and the contribution claims

1 that they could otherwise assert against the settling party is
2 dismissed. What Mr. Basta didn't read is that the other
3 protection in 15-108 is that the reduction of the nonsettling
4 parties is reduced by the greater of the consideration paid by
5 the settling party or the proportionate share of fault that the
6 other party had in the transaction, whichever is greater,
7 translated to this situation. If this section applies, which I
8 do not think it applies, and we cited the AMT Mobile case, a
9 Judge Shannon decision, 404 B.R. 118, which specifically said
10 that joint tortfeasor liability doesn't apply in a fraudulent
11 transfer case. And I don't think any of their cases are
12 fraudulent transfer cases. But if this section applied then if
13 LCPI was deemed to be a joint tortfeasor with LBREP and LCPI
14 was fifty percent at fault, and even though they're paying
15 something less than the fifty percent exposure, LBREP's
16 exposure to the SunCal trustee has been reduced by fifty
17 percent because it gets reduced by the greater of the dollars
18 or the equitable share.

19 THE COURT: So you're saying the settlement benefits
20 them.

21 MR. STEINBERG: Absolutely benefits them. And the
22 thing that he spent ten minutes railing about is because he
23 didn't fully read the section. The section says you get the
24 benefit of the proportionate fault. That's why the
25 contribution claims go away under this section if this section

1 applied. But it doesn't apply because we're not asserting a
2 contribution claim against them. We're asserting a deficiency
3 claim against the SunCal estate. We made a loan on the first
4 lien basis for 235 million dollars. Our collateral would be
5 worth less than a hundred million dollars. We have a
6 deficiency claim for over 200 million dollars. And we're
7 filing it in the case for whatever it comes out to be. And
8 we're actually reducing what our share otherwise would be as an
9 additional benefit to the SunCal trustee to promote the
10 settlement.

11 So this -- you could try to squeeze as much as you can
12 the square peg into the round hole. But there's no litigation.
13 We haven't asserted any direct claims against them and we're
14 not. We're asserting a claim for a deficiency on a 235 million
15 dollar loan that's filed against them. And let's just put it
16 on the table. The fifty-fifty split, the LCPI share of the
17 fifty-fifty split is fifteen percent, right, with thirty
18 percent of the first lien debt. Our share is fifteen percent.
19 If Gramercy is correct that it doesn't apply to the other
20 recoveries then our share is even going to go down much further
21 than that because the second lienholders and the third
22 lienholders are going to participate in the settlement and
23 we're going to have to contribute more of what the other
24 recoveries are in order to effectuate the fifty-fifty split
25 which is part of this transaction.

1 So no one is profiting. They're giving up. And the
2 question asked, why are we giving up -- why are we asking for
3 other recoveries which we think has merit -- well, we agree.
4 We don't think the lawsuit had merit. So at the end of the
5 day, there will be nothing paid by LBREP. They'll win.
6 They'll vindicate itself. We think they will. And we won't
7 get anything on the other recoveries. And so be it. That's
8 the element of the deal that we captured. And all of this
9 fifty-fifty split is something that's embedded in the plan.
10 Ultimately, it will have to be approved by the SunCal
11 bankruptcy court in connection with the SunCal plan of
12 reorganization.

13 THE COURT: Let me ask you a question that's very,
14 very basic and follows on your last comment. My approval of
15 this settlement doesn't really effectuate the settlement. It
16 simply is the first step in a process that we discussed on the
17 phone earlier with Mr. Smiley that may lead to a settlement
18 which is a confirmed plan of reorganization which is built on
19 the settlement. Do I understand that correctly?

20 MR. STEINBERG: Yes and no, Your Honor. There are --
21 if you approve the settlement and the California bankruptcy
22 court approves the settlement, then we will have a settlement
23 effective date and certain rights will flow from the settlement
24 effective date. Then there's a contractual obligation by the
25 trustee under the settlement which has been approved --

1 THE COURT: To prosecute the plan.

2 MR. STEINBERG: -- to proffer a plan which will have
3 the elements about selling the property and provide for the
4 fifty-fifty recoveries -- fifty-fifty sharing in other
5 recoveries. That's embedded in the plan. The term sheet also
6 provides that if the trustee can't consummate that plan within
7 a certain period of time, it specifies what the recoveries --
8 what happens as a result of that. We can then move forward on
9 a foreclosure and they're not going to contest it which will
10 allow us to be able to sell the properties. And the issue
11 about the other recoveries will be left open in the SunCal
12 court to try to figure out.

13 THE COURT: Okay.

14 MR. STEINBERG: So, Your Honor, the purpose of 108 is
15 to facilitate settlements. It's to allow this type of
16 circumstance. It provides that they will get a benefit of the
17 equitable share.

18 I will just say briefly on the second lien agent.
19 They asked for specific language in the order that said
20 notwithstanding anything in the contrary in the amended term
21 sheet in this order, nothing in the amended term sheet is
22 intended to affect the rights of any -- of any person including
23 the second lien lenders. So what is it that he thinks he's
24 still objecting to? He got the provision that says we're not
25 trying to interfere by this approval order of anything relating

1 to the intercreditor agreement. I will also say that if you
2 read his objection, you'll never find this argument. He
3 doesn't talk about that there may be a potential violation of
4 the intercreditor agreement. And reading the declaration of
5 Robert Brusco, which is basically -- encapsulates the moving
6 brief, that's nothing illuminating for purposes of him making
7 this argument. Whatever was on the table with regard to other
8 recoveries was on the table when we filed this motion and all
9 along.

10 So, I think what you got here was a shuffle by a
11 lawyer when he had nothing to say. There was nothing in his
12 objection. He always had notice of it. There's nothing about
13 that he's arguing about a violation of the intercreditor
14 agreement. He couldn't articulate what it was. And he
15 bargained for a provision that says we're not trying to affect
16 the intercreditor agreement. Frankly, I think what he does, as
17 I said before, there are general provisions in the
18 intercreditor agreement which talk about what the second lien
19 lender can do or can't do vis-a-vis the first lien lender. And
20 I think he's probably coming fairly close once he abandoned the
21 helpful suggestions and is now trying to make a more direct
22 claim.

23 So, Your Honor, I think that's my response to the
24 remaining responses.

25 THE COURT: Okay. Mr. Basta, I'm going to give you an

1 opportunity. I just have a procedural question. Mr.
2 Steinberg, you mentioned the declaration which is going to be
3 presumably the subject of some further examination. Do you
4 wish, in connection with affirmative case, to put your
5 declarant on the stand or do you simply want to expose him to
6 cross-examination?

7 MR. STEINBERG: I think, Your Honor, expose him to
8 cross-examination.

9 THE COURT: Okay. Mr. Basta?

10 MR. BASTA: I just have one point to respond to
11 because I checked my reading skills because I read the statute
12 again. And the statute doesn't say that if we get the benefit
13 of a reduction that we have to -- the statute doesn't say that
14 we have to choose between (a) and (c). The statute says, we
15 get (a) and the statute says we get (c). They're
16 comprehensive. It's (a), (b) and (c). It's a package. I
17 understand we get the benefit of (a). We get the benefit of
18 (a). Now the benefit of (a) isn't going to reduce litigation.
19 It's going to increase litigation because we're going to be
20 sitting here at some point in time potentially arguing over
21 relative contribution. But that -- just because there's a
22 reduction in the greater of the settlement amount and the
23 equitable share of damages doesn't right out (b) and (c) which
24 all the case law says embodies a quid pro quo arrangement. And
25 that quid pro quo arrangement -- they haven't said anything to

1 suggest that the statute doesn't apply. Judge Shannon never
2 said in AMT case that the statute doesn't apply. All Judge
3 Shannon said is that in a fraudulent conveyance action where
4 the only cause of action is a rescission and return, he
5 wondered whether or not there was really contribution in that
6 context. The complaint that the trustee has been threatening
7 with us has all sorts of causes of action, you know, brief of
8 fiduciary duty, the same stuff that they threw at these guys.
9 And so, to suggest that we're not going to be in a position
10 where this contribution principle is coming down the pike, I
11 just don't think they made a case that to show that we're not
12 going to be harmed by the structure of this settlement.

13 THE COURT: But to be clear, Mr. Basta, the reason
14 that you're objecting to the settlement is not that the
15 settlement fails to deliver everything that LCPI should want in
16 a settlement.

17 MR. BASTA: Right.

18 THE COURT: But rather that the settlement carries
19 with it what you view as the negative collateral damage
20 potentially to your client. Is that right?

21 MR. BASTA: I think that we read Drexel and a RICO
22 that says when approving a settlement, the Court should
23 consider the impact on nonsettling defendants. And in my
24 view -- in our view -- not my view; in our view, a settlement
25 that ignores the impact of state law on how the contribution

1 claims work, a settlement that does not follow that state law,
2 I don't know how that settlement can satisfy 9019. So I don't
3 think it's a situation --

4 THE COURT: But you're one step removed from that.
5 Very frequently, a 9019 settlement is settling litigation --

6 MR. BASTA: Right.

7 THE COURT: -- or settling potential litigation --

8 MR. BASTA: Right.

9 THE COURT: -- which is litigation that would be
10 pursued within the bankruptcy court that is approving the
11 settlement. Here, you're complaining about potential
12 collateral damage impact to your client in California of a
13 litigation that hasn't been brought but it has been threatened.
14 And it's being settled as it relates to LCPI. And your
15 objection is that if that litigation is never pursued, there
16 may be a negative impact to the extent that California law
17 follows 5108's provisions although we haven't been cited to and
18 I don't have a copy of the California statute that undoubtedly
19 would be the statute that Judge Smith will be looking at. So
20 we've been making an argument about New York law that probably
21 doesn't apply --

22 MR. BASTA: Right.

23 THE COURT: -- in California bankruptcy court.

24 MR. BASTA: Your Honor --

25 THE COURT: Do I have that right?

1 MR. BASTA: Look, I think you have the following
2 right.

3 THE COURT: Did I summarize the position correctly?

4 MR. BASTA: No. I don't believe you summarized --
5 with all due respect, I just don't think you summarized the
6 position correctly. I think we're here to approve a
7 settlement.

8 THE COURT: You're here to block a settlement because
9 you think it's advantageous to your client to break the play
10 and be in the room so that you can get into a comprehensive
11 settlement that benefits your limited partners, isn't that
12 right?

13 MR. BASTA: Yes. And it's also right that Lehman is
14 the general partner. But I am suggesting, Your Honor, that the
15 settlement structure itself doesn't comply with state law.
16 Now, Your Honor can say, Mr. Basta, go take that to California.

17 THE COURT: I could say that.

18 MR. BASTA: Yes. You could say that. And we'll go
19 to California if Your Honor says that. I don't know why I have
20 to go here and I have to go to California. If I have to go to
21 California, I will. My client is, I think, entitled to take
22 actions that it thinks will benefit -- in fact, has a duty to
23 its limited partners to do so. And here, I don't think this is
24 a question of there's a statute. And the statute says how it
25 works. And the statute says that they can't take an interest

1 in the claim against us relating to their own conduct that
2 they're settling. And so we're here to bring that statute to
3 the Court's attention and say go and structure the settlement
4 in a manner that does not eliminate our contribution claim
5 against them and does not incent the lenders and LCPI who
6 bought their debt with a view to solvency to have a financial
7 interest in -- they have a financial interest in their own
8 conduct.

9 THE COURT: Okay.

10 MR. BASTA: Thank you, Your Honor.

11 THE COURT: Now are we going to pursue the Gramercy
12 objections?

13 MR. DURRER: We're ready, Your Honor.

14 THE COURT: Let's call your witness.

15 MR. DURRER: Your Honor, we would -- Mr. Brusco's
16 here.

17 (Pause)

18 THE COURT: Please raise your right hand.

19 (Witness sworn)

20 THE COURT: Be seated, please.

21 MR. DURRER: Good afternoon again, Your Honor. Van
22 Durrer, Skadden, Arps, Slate, Meagher & Flom, on behalf of
23 Gramercy Warehouse Funding I LLC.

24 CROSS-EXAMINATION

25 BY MR. DURRER:

1 Q. Good afternoon, Mr. Brusco.

2 A. Good afternoon.

3 Q. Are you familiar with the declaration that you -- that was
4 submitted as signed by you in connection with this contested
5 matter?

6 A. Yes, I am.

7 Q. Have you read your declaration fully?

8 A. Yes, I have.

9 Q. Do you have a copy of your declaration with you?

10 A. Not here but --

11 Q. I have extra copies --

12 A. -- I'm sure there's plenty of copies in the courtroom.

13 Q. Yeah. I just --

14 MR. DURRER: It might be convenient, Your Honor --

15 THE COURT: You may approach and give him a copy of
16 his declaration.

17 MR. DURRER: Thank you, Your Honor.

18 THE WITNESS: Thank you.

19 MR. DURRER: Would you like an extra copy of it?

20 THE COURT: Sure.

21 (Pause)

22 THE COURT: Thanks.

23 (Pause)

24 Q. Mr. Brusco, in your -- actually, let me ask you a few
25 background questions first. Do you hold any professional

1 licenses?

2 A. Yes. I hold a law license.

3 Q. For which state?

4 A. New York and New Jersey.

5 Q. And are you a practicing attorney?

6 A. I am not.

7 Q. When were you admitted to the bar in New York and New
8 Jersey, sir?

9 A. 90 -- 1992.

10 Q. What is your position with LAMCO?

11 A. I am senior vice president.

12 Q. Okay. And your declaration states that you're the person
13 primarily responsible for the direct management of SunCal
14 loans. I want to ask you specifically, does that include
15 directing and consulting with counsel for LCPI in connection
16 with the SunCal bankruptcy cases in California?

17 A. Which SunCal bankruptcy cases? There are a number of
18 them.

19 Q. The SunCal bankruptcy cases that are the subject of this
20 settlement.

21 A. Yes.

22 Q. Does it also include the SunCal cases that are not the
23 subject of this settlement?

24 A. Yes.

25 Q. Okay. And is it also within your responsibilities to

1 consult and direct King & Spalding in connection with the
2 motion that is before the Court today in these bankruptcy cases
3 in New York?

4 A. Yes. But I would add that I do that in consultation with
5 our internal committee as well as Alvarez & Marsal who is our
6 restructuring officer.

7 Q. And who are the members of the internal committee you just
8 referred to?

9 A. The --

10 MR. PEREZ: Your Honor, I'm going to let him go a
11 little bit of background. But this has nothing to do with any
12 of his objections and I don't believe is relevant.

13 THE COURT: I totally agree. I'm finding this pretty
14 far afield. And this isn't a deposition. This is the pursuit
15 of focused questioning in support of whatever are your
16 remaining objections. So no latitude. Go to the points.

17 MR. DURRER: For purposes of the record, Your Honor,
18 may I make a proffer of where I'm heading with this?

19 THE COURT: Sure.

20 MR. DURRER: Thank you, Your Honor. Your Honor, as we
21 mentioned during the earlier comments, we have concerns that
22 the settlement is not fair and is not entered into in good
23 faith. The process by which the witness who is in control of
24 that process went about that process is directly relevant to
25 that inquiry.

1 THE COURT: Yes. But the only basis that gives you a
2 reason to stand at the podium is your strained allegation that
3 there's something about this settlement that may result in a
4 breach of an intercreditor agreement. You don't have a
5 generalized fishing expedition to pursue unsubstantiated
6 allegations of lack of good faith. And this is not going to
7 happen this afternoon. It's 3 o'clock. I've been on the bench
8 since 10 o'clock this morning. You're going to get an
9 opportunity to ask focused questions only.

10 MR. DURRER: I appreciate that, Your Honor. May --

11 THE COURT: Go ahead.

12 MR. DURRER: May I finish with my proffer?

13 THE COURT: Ask your questions.

14 MR. DURRER: Your Honor, respectfully --

15 THE COURT: Respectfully, you're on thin ice.

16 MR. DURRER: I understand, Your Honor.

17 THE COURT: You have barely standing to be here. Ask
18 your questions.

19 BY MR. DURRER:

20 Q. Mr. Brusco, how did you value the various components of
21 the settlement? And by components of the settlement, I mean
22 the consideration that is being offered and obtained by LCPI in
23 connection with the settlement?

24 MR. PEREZ: Your Honor, I'm going to object. It goes
25 beyond the scope of his objection. I mean, he objected on

1 three grounds, two of which were addressed. We think we
2 addressed the third. The third was the helpful suggestion --
3 if you look at what his objections are, valuing the components
4 of the settlement had absolutely nothing to do with anything
5 that he raised nor touched neither topside nor bottom.

6 THE COURT: Sustained.

7 MR. DURRER: Your Honor, the relief we seek --

8 THE COURT: You don't seek relief. You're objecting
9 to a settlement.

10 MR. DURRER: We're objecting to the settlement unless
11 it is approved on the condition that there be a fair process.
12 That is exactly consistent with the comments I made about this
13 settlement not being fair and not being entered into in good
14 faith. If I --

15 THE COURT: You didn't raise an objection to the
16 settlement that it wasn't entered into in good faith.

17 MR. DURRER: We didn't have Mr. Brusco's declaration
18 which refers to his internal approval.

19 THE COURT: Mr. Brusco's declaration tracks the
20 motion.

21 MR. DURRER: Mr. Brusco's declaration refers to
22 internal approvals. And that process, we believe, ends with
23 two people, Mr. Huesen (ph.) and Mr. Walsh. It ends with the
24 same people for both sides of this controversy --

25 MR. PEREZ: Well --

1 MR. DURRER: -- for the LBREP side and for their side.
2 I won't have the opportunity in California to explore that
3 because when I seek to depose Mr. Brusco, when I object to the
4 settlement there that was just filed yesterday, these gentlemen
5 and Mr. Troop, who I don't know if he's still here for
6 Cadwalader, will object and say you can't discovery because of
7 the automatic stay. The relief that we -- the condition that
8 we suggested would be appropriate for approval of the
9 settlement today was to either give us the opportunity to take
10 that discovery and we're happy to discuss how it be limited, or
11 alternatively, pick a third party impartial, subject to Your
12 Honor's jurisdiction, and we will live with it. If the person
13 says the deal's good, there's no lawsuit, we will live with
14 that. As to the expense issue, we're happy to have the expense
15 shared by the two estates. We thought Your Honor would prefer
16 to have control of that person. That I'm trying -- and I
17 appreciate the Court's indulgence in allowing me to explain how
18 this is related to the settlement not being in good faith and
19 fair if we don't have that opportunity. If Your Honor enters
20 the form of order that we proffered, either option, then we
21 have no further objection to the settlement in this court. But
22 we feel that if it goes forward with one -- both arms tied
23 behind my back in California, that is unfair. It does affect
24 my rights and it's not in good faith.

25 THE COURT: Look, you're making an argument in the

1 middle of examining a witness. You wanted to examine the
2 witness. You can ask proper questions of the witness. There's
3 been an objection to the question which I sustained. You can
4 ask proper questions. No speeches.

5 MR. DURRER: I appreciate that, Your Honor.

6 THE COURT: No speeches now.

7 MR. DURRER: Thank you, Your Honor.

8 BY MR. DURRER:

9 Q. In connection with entering into the settlement, there
10 were no discussions, consultations, negotiations with Gramercy
11 on the LCPI side, is that correct?

12 A. In connection with the settlement at issue, the answer is
13 yes. There were no discussions with Gramercy.

14 Q. Or any discussions with any of the third lien lenders
15 other than LCPI itself?

16 A. There were not.

17 Q. Your declaration refers to your experience and opinions.
18 And your opinions -- in your opinion, would it be beneficial,
19 in general, to have consensus in connection with a settlement
20 like this?

21 MR. PEREZ: Objection, Your Honor. I'm not sure that
22 I understand the question. So I would object to it as being
23 vague.

24 THE COURT: Why don't you rephrase the question?

25 MR. DURRER: Thank you, Your Honor.

1 Q. In general, do you think it would be helpful and
2 beneficial to have universal consensus in connection with the
3 settlement when entering into a settlement?

4 MR. PEREZ: Same objection, Your Honor.

5 THE COURT: Sustained. It's not tethered to
6 particular facts. Of course it's always best if you have
7 universal consensus and everybody sings Kumbaya. That's not
8 required, however.

9 MR. DURRER: Certainly not, Your Honor. I agree.

10 Q. In connection with this settlement, would it be beneficial
11 to have universal consensus?

12 A. Well, I don't think I can say it more adequately than the
13 judge just said it. But yes, in a perfect world, I think it's
14 nice to have consensus by all parties. I don't think that's
15 necessary required in this case. I think we've structured a
16 settlement that will get us to where at least LCPI and the
17 trustee need to get to in order to effectuate the settlement we
18 bargained for.

19 Q. In fact, wasn't it a substantial factor weighing in favor
20 of your determination to enter into the settlement that it
21 would avoid future litigation?

22 MR. PEREZ: Your Honor, I don't think that's -- I
23 think we say that in our pleading. This is not an area that is
24 of any contention. I don't know that this is intended to
25 impeach the witness. The matter is just repetitive. And it

1 doesn't go to any issue that is contested in this matter.

2 THE COURT: I agree. I think it would be useful to
3 focus on whatever it is you want to focus on in support of your
4 remaining objection.

5 Q. In assessing your business judgment to approve this
6 settlement, did you take into account the potential for
7 liability on an administrative basis for breach of the
8 intercreditor agreement?

9 A. Can you repeat that?

10 Q. Yes. Are you --

11 MR. DURRER: I'll rephrase the question, Your Honor.

12 Q. Are you familiar with the intercreditor agreement entered
13 into in 2007 among the lenders in connection with the SunCal
14 loans that are the subject of the settlement?

15 A. I am familiar that an intercreditor agreement exists, yes.

16 Q. Okay. In considering whether to enter into this
17 settlement, did you consider potential exposure under that
18 intercreditor agreement?

19 A. Yes. There were discussions with counsel.

20 Q. How did you evaluate your potential exposure on the
21 intercreditor agreement?

22 MR. PEREZ: Two objections, Your Honor. First, I
23 mean, I think he indicated that there were discussions with
24 counsel. So I would object based on attorney/client privilege.
25 But more fundamentally, there's nothing in his papers about a

1 violation of the intercreditor agreement or any such thing so
2 it really is beyond the scope of his objection.

3 THE COURT: Sustained on both grounds.

4 MR. DURRER: Your Honor, with respect to the counsel
5 argument, the declaration specifically states that it is based
6 on discussions with counsel.

7 THE COURT: It's not a waiver. This isn't an at-issue
8 waiver.

9 Q. In paragraph 25 of your declaration, you state that you
10 believe that LCPI has valid defenses to the claims and the
11 SunCal trustee. What are those valid defenses as you understand
12 them?

13 MR. PEREZ: Your Honor, again, not -- it wasn't
14 included in any of his pleadings. In our reply, we go to great
15 lengths in a footnote to cite exactly what we had said in the
16 California case indicating all of the reasons why we thought it
17 was there. Again, I don't think that there's any issue, hasn't
18 been raised by him. And it's not something that is in dispute
19 in this case. Yes. They -- counsel did file -- or his
20 predecessor counsel did file a fraudulent conveyance claim.
21 And the position that LCPI has taken has been consistent since
22 November of 2008.

23 THE COURT: I'll sustain the objection and consider
24 that the examination is running so far afield of any cognizable
25 objection that this is beginning to look like a fishing

1 expedition. Please, if you have a valid objection to the
2 settlement, ask questions about that that go to this man's
3 business judgment.

4 MR. DURRER: I believe I inquired into the exercise of
5 his business judgment and that calculus and how he evaluated
6 the various components to the settlement. And I believe that
7 Your Honor sustained an objection to that.

8 THE COURT: What I'm telling you is that this man is
9 being called as a witness in connection with his declaration.
10 You can ask him questions that fit within cross-examination of
11 that declaration in connection with his role as a witness in
12 support of a 9019 settlement which is being proffered by virtue
13 of the debtors' business judgment that this is in the best
14 interest of the LCPI estate. If you have objections to that,
15 you can raise such objections. Or, if you have objections that
16 this somehow prejudices your client, you can raise such
17 objections but only to the extent that it's within the scope of
18 the declaration, because that's his direct testimony.

19 MR. DURRER: Okay.

20 BY MR. VAN DURRER:

21 Q. The settlement calls for the SunCal trustee to receive 3.5
22 percent of net proceeds from the sale of the collateral, is
23 that correct?

24 A. That is correct.

25 Q. How do you value that consideration to the trustee?

1 A. Are you asking me how is that monetized?

2 Q. What do you think it's worth?

3 A. Well, I can give you an example. I mean, the appraised
4 values of the properties was sixty-two million. Okay? I mean,
5 I can do the math for you if you'd like.

6 Q. Is it your testimony that you believe that that's worth
7 sixty-two million times .035?

8 A. Well, it's supposed to be a net -- it's supposed to be
9 three and a half of net proceeds. So it would be whatever the
10 sale proceeds are. I think in this case you have to calculate
11 deductions of senior liens in order to satisfy the senior
12 liens, you know, broker costs, all that stuff. You net that
13 out and then the trustee would take home three and a half
14 percent of that net number.

15 Q. And in connection with your evaluation of the settlement,
16 did you do that calculation?

17 A. At one point in time, yes, we did.

18 Q. Okay. And what was the result of that calculation?

19 MR. PEREZ: Your Honor, I think that calls for the
20 witness do disclose what he thinks the value of the property
21 is. There's three pieces of testimony in the record indicating
22 value. There's the forty-one million dollar offer that was
23 made that Mr. Smiley referred to. There's a forty-five million
24 dollar credit bid which we're doing. And then there's the
25 appraised value which was indicated in what was filed in the

1 California cases. For Mr. Brusco to talk about where he thinks
2 it's going to end up, first of all, doesn't go to any issue in
3 the case. It doesn't go to any issue raised by Gramercy in the
4 case and would just divulge confidential and proprietary
5 information as to what Lehman thinks or LCPI thinks is the
6 value of the case.

7 Furthermore, Your Honor, nobody is saying -- I haven't
8 heard anybody say you're either getting too much or you're not
9 getting enough. This is strictly a fishing expedition.

10 THE COURT: I'll sustain the objection. I have yet to
11 hear a question that goes to the heart of any objection. And
12 it really seems to be something that amounts to a deposition
13 and I can't tell if it's being used for purposes of this
14 bankruptcy or if it's being used for purposes of the other
15 bankruptcy where you claim that you can't take discovery
16 because of the impact of the automatic stay. If that's your
17 objective here, this is really a misappropriation of the
18 Court's time.

19 MR. DURRER: Well, I certainly don't want to do that,
20 Your Honor. I have two questions, very specific questions.

21 BY MR. DURRER:

22 Q. Have you permitted your counsel in the SunCal bankruptcy
23 case that is the subject of this settlement to engage in any
24 discovery where they offer documents respond to discovery?

25 A. By any party?

1 Q. By any party.

2 A. I believe the answer is yes. We've actually -- I believe
3 we've actually given discovery to the SunCal trustee.

4 Q. In response to discovery requests in litigation?

5 A. I'd have to defer to counsel on that. I just don't recall
6 whether it was in direct response to discovery demands that
7 were made or it was more in a cooperative nature. I just don't
8 recall.

9 Q. And why have you not engaged in conversations, discussions
10 or negotiations with Gramercy in connection with this
11 settlement?

12 MR. PEREZ: Objection, Your Honor. Irrelevant.

13 THE COURT: Sustained.

14 MR. DURRER: Your Honor, that question goes directly
15 to our allegation of bad faith.

16 THE COURT: Well, it may also go to whether or not
17 Gramercy filed a motion for relief from stay with focused
18 discovery for particular purposes either in this court or in
19 the California court. I know from my experience that no such
20 requests for stay relief were made here. It may be that the
21 answer to the question is because nobody asked the questions
22 the right way. I don't think that you are doing anything that
23 helps your objections. And I am increasingly convinced by your
24 questions that you're pursuing another agenda here unrelated to
25 any objection to the settlement. And I'm not real happy about

1 that.

2 MR. DURRER: Your Honor, there is no other agenda.
3 Candidly, we just want the opportunity to explore the
4 settlement on its merits in the California court. We believe
5 we're going to be prevented from doing so.

6 THE COURT: Well, I think you'll have that opportunity
7 if you make a proper request to Judge Smith.

8 MR. DURRER: Thank you, Your Honor. I don't have any
9 other further questions.

10 THE COURT: Okay. Does anybody else wish to question
11 the witness?

12 MR. PEREZ: I have nothing, Your Honor.

13 THE COURT: You're excused, Mr. Brusco.

14 (Witness excused)

15 THE WITNESS: Thank you, Your Honor.

16 THE COURT: Is there anything more on this?

17 MR. BASTA: Not from our end, Your Honor.

18 MR. COHEN: Your Honor, just to put the -- Fidelity's
19 reservation of rights that we've deferred from earlier onto the
20 record, there is -- as has been discussed, part of the
21 settlement has the disbursement of the development account
22 funds. And as we articulate in our limited objection, Your
23 Honor, the disbursement of those funds may negatively impact
24 the availability of coverage under Fidelity's title insurance
25 policies. We've made LCPI aware of that not just in

1 conjunction with this particular proceeding but in prior
2 proceedings. And we assume that as part of the calculus in
3 going to the business judgment to consider the settlement. And
4 we just reserve our rights with respect to any impact that the
5 proposed settlement has on availability of coverage under the
6 policies. And we'll defer that issue to a later date.

7 THE COURT: Okay.

8 MR. COHEN: Thank you, Your Honor.

9 MR. PEREZ: Your Honor, we did file -- I'm sorry -- a
10 revised proposed form of order. I don't know whether the Court
11 was able to see that. But I can say I have copies to hand up
12 to the Court.

13 THE COURT: Why don't you hand that up? Thank you.

14 MR. PEREZ: In particular, Your Honor, that does
15 include both -- I think it's on the third page. The first one
16 is the marked -- on the third page of the order, it does have
17 the reservation of rights and the statement that nothing herein
18 affects -- that nothing herein is intended to affect the rights
19 of any third person including the second lienholders and that
20 only the parties to the term sheet's rights are affected. And
21 secondly, Your Honor, the other major paragraph is the tolling
22 of the statute of limitations. And then the third item was
23 also in response to Mr. Durrer's comments about concurrent
24 jurisdiction of both bankruptcy courts.

25 THE COURT: Okay. The SunCal bankruptcy cases, for

1 some reason, have become a major distraction on here. And
2 that's not just in this afternoon's argument but, frankly,
3 throughout these proceedings including a matter in an unrelated
4 case which is already on appeal to the Second Circuit.

5 The settlement which is currently before the Court is
6 actually the direct result of certain statements that I made
7 from the bench in the context of a motion brought by the SunCal
8 Chapter 11 trustee for relief from the automatic stay in order
9 to pursue litigation claims against LCPI in California and to
10 sell certain property in California while depriving LCPI of its
11 right to credit bid.

12 During the course of the argument that I believe took
13 place in July of this year with respect to that motion for
14 relief from the stay, I noted that a term sheet had been
15 developed many months prior to the date of that hearing which
16 provided for, among other things, the development of a plan of
17 reorganization with the support of LCPI that would have
18 provided for a sale of the property under a confirmed plan of
19 reorganization. In effect, the current term sheet builds on
20 that prior document and with some modifications including those
21 that have been identified by Mr. Steinberg in his remarks.
22 This is a result that has been long in the making.

23 It comes as something of a surprise to me that third
24 parties who appear not to be directly impacted by the
25 settlement have raised objections some creatively going into

1 the question of whether or not joint tortfeasor law is somehow
2 implicated in a negative way by the settlement. I recognize,
3 and I think I said this during my conversations with Mr. Basta,
4 that the motivation here may be to derail the settlement so
5 that settlement discussions can take place with more parties
6 embraced by the settlement in a more comprehensive settlement.
7 Moving counsel for Gramercy, when asking questions of Mr.
8 Brusco, made a general reference to the fact that it would be
9 more favorable if the settlement embraced more parties. And I
10 recognize that as true. It probably would be more favorable if
11 the settlement embraced more parties. But the settlement in
12 the form that it has been presented is nonetheless one that
13 LCPI, through counsel and through Mr. Brusco, has urged that
14 the Court approve because it benefits the estate.

15 The creditors' committee filed papers in support of
16 the settlement although counsel for the committee has not
17 spoken in connection with today's contested hearing. I have
18 reviewed the committee's papers and recognize that the
19 committee is, in effect, a strong supporter of approval of the
20 settlement.

21 I'm prepared to approve it. And I'm sure that comes
22 as no surprise to the objectors. But I am concerned about some
23 of the arguments that had been made in respect of the joint
24 tortfeasor problem in particular. And I'm simply going to
25 reserve the time for entry of the order so that I can more

1 fully examine the cases that have been cited both by LBREP and
2 by LCPI on the subject of the applicability of these various
3 cases and also the standards applicable to third parties
4 claiming potential damage on account of a settlement.

5 I don't see a clear connection between this settlement
6 and the damage alleged by LBREP, but I want to give it some
7 more thought. It also occurs to me that the proper form for
8 raising many of these issues is the bankruptcy court in Santa
9 Anna, California when the settlement will be presented to Judge
10 Smith and when there will also be a plan process that will
11 allow parties who can legitimately demonstrate that they are
12 adversely affected by this to have their day in court. So I'm
13 going to give this some more thought. But the clear indication
14 that you should take away from this is that the objections are
15 going to be, in all likelihood, overruled, that the settlement,
16 in all likelihood, be approved and that I'll take appropriate
17 action in connection with the proposed form of order as
18 promptly as I can do that.

19 To the extent that any party may wish to submit
20 anything in addition to what has already been presented today
21 in the form of a letter brief, my suggestion is that that be
22 done by no later than September 27 which is next Monday. I'm
23 not encouraging that that be done. I'm simply noting that if
24 you feel that there is something more than needs to be brought
25 to my attention while I'm thinking about this that that will be

1 your last and best opportunity to do that.

2 We're adjourned.

3 (Whereupon these proceedings were concluded at 3:25 p.m.)

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I N D E X

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C E R T I F I C A T I O N

I, Clara Rubin, certify that the foregoing transcript is a true
and accurate record of the proceedings.

Clara Rubin

AAERT Certified Electronic Transcriber (CET**D-491)

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Date: September 24, 2010